



BUSINESS-DRIVEN INNOVATION



# Tackling 3 Critical Challenges to Achieve & Surpass IFRS 17 Compliance

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# The countdown for IFRS 17 has begun... Are you prepared?

The incoming set of new accounting standards are the biggest reporting changes for life insurers in more than a generation—requiring the creation of a long-term roadmap uniting finance, risk and actuarial teams, as well as significant data and technology innovation.

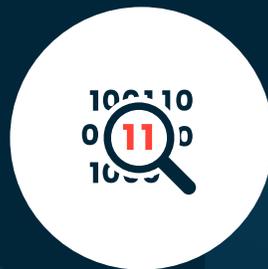
## Making sure your company is compliant is key.

In this eBook, we'll explore leading opinions on the three critical areas that insurers need to address in order to become IFRS 17 compliant by the January 01, 2023 deadline.



Critical Challenge #1

# The Data Challenge



# Solving the IFRS 17 Data Challenge for Life Insurance Leaders

IFRS 17 is being billed as the biggest set of accounting standard changes to hit the insurance industry in 15 years—posing significant data challenges to organizations attempting to achieve compliance ahead of the looming January 1, 2023 deadline.

The sweeping new set of standards will require calculations to be made on every policy, including projections on future premiums, claims and reinsurance. Policies will need to be evaluated in terms of their profitability. And judgements will have to be made on how policies fit into portfolios, groups and cohorts.

## To accomplish that, organizations will need to be able to:

- ▶ Access all of their policy data in their insurance, accounting and actuarial systems
- ▶ Clean, convert and extract important values from data at the right level of granularity
- ▶ Implement an automated process for moving data through transformations from source to reporting



**For most insurers, meeting these challenges will require new ways of thinking, technology and expertise.**

## Data challenge #1: Access to all data

The first challenge is that the data needed to generate IFRS 17 compliant reports resides in different systems in the organization—including the policy administration, actuarial and accounting systems. The disparate sources and the complexity in mapping mean that, at its core, IFRS17 reporting becomes a “data” problem.

Gaining access to the data in those systems is complicated by the fact that almost all life insurance companies are working off multiple legacy back office systems that can be decades old. These systems present obstacles to easy data access. They may be disconnected and don't allow easy data retrieval. This creates data silos and shadow IT solutions because they often require the application of unique manual processes to access data—which is inefficient, expensive and error prone.

**“ In too many cases, just accessing the necessary data is a form of technological archaeology—painstaking manual work that is more complex than it needs to be. ”**

The amount of data migration and conversion required to access what will be needed to comply with IFRS 17 is staggering. And, as with any migration, using traditional methodologies for conversion creates significant risk in a project that has a tight and non-negotiable deadline.

The risks generated by old ways of migrating data—loss or corruption of data, fear of a data breach, maintaining parallel systems—are big enough that they have long been one of the main reasons why carriers haven't modernized their policy administration systems.

## Data challenge #2: Standardization and granularity

Another key data challenge is that, often the data is not organized in a way that can be easily consumed and processed. Data is not necessarily standardized or interrelate-able across systems, making it difficult to merge into a single usable data set without creating data integrity issues.

And that's just the data in the core systems. The matter is complicated by the fact that much of the required data resides in spreadsheets and other ad-hoc data sources. Many actuaries, for example, work off excel templates that use data manually sourced from systems other than their own and aren't easy to integrate with.

Data standardization and the ability to extract the values you require at the right level of granularity, are an area of weakness for many companies—especially those who are multinationals or have engaged in a lot of M&A activity over the years. The problem grows when you consider that some life insurance contracts last almost a lifetime and the decades old data within may be structured in different formats over time.

**“ A company’s enterprise-wide data set is not likely to have the consistency needed for use in IFRS 17 calculations, unless they have been extraordinarily vigilant in maintaining a strict standard over long periods of time. ”**

## Data challenge #3: Defining the Data Process

The third data challenge created by IFRS 17 is defining the process for moving data from source to reporting. Under previous regulations, that process was a lot more straightforward.

Since revenue was recorded by posting premiums directly to the P&L, there were relatively few steps involved. Under IFRS 17, data must be accessed, then processed—transforming as it passes between different systems in order to perform the calculations necessary to generate compliant reports. The steps in the process must be well-defined, and most importantly, they must be automated.

IFRS 17 compliance will create nightmares for organizations that end up introducing a host of new manual process that must be completed to achieve compliance.



The right automated process should enable staff to focus on high-value tasks like analysis and providing strategic input to different product lines.

Implementing the most effective and least disruptive process will require insurers to choose the right technology and conversion methodologies. This will ensure steps are automated, data risk is eliminated, and the end product is useful, not just for required reports, but to improve company-wide decision-making and accelerate innovation.

## Succeeding & Surpassing IFRS 17 Standards – The IFRS 17 Data Solution

What insurer's need to solve their IFRS 17 data challenges is the right set of tools that allow them to source their data in an efficient and effective way. These tools enable a company to manage the problem of how their data is inter-related data using an industry standard data model.

This kind of data model allows an organization to evaluate where each of group of data can be sourced from and access it at whatever level of granularity each system provides.

Through data-quality metrics and data massaging techniques, it enables each instance of source data to be related to the others. That way, widely disparate types of data that started at different levels of granularity can all be used for analysis.

Overcoming the significant data challenges presented by IFRS 17 will require the implementation of a solid insurance data foundation, good data integration techniques and the help of the right data integration partners.

For insurers already thinking about the need to modernize their policy administration systems to accelerate innovation, increase operational efficiencies and provide superior customer experiences, IFRS 17 may be the tipping point to making the decision to implement a rules-based PAS.

**Critical Challenge #2**

# Choosing the Right Measurement Models for Success



# Choosing the right measurement approach is a data problem

The three measurement approaches allowed by IFRS 17 describe how a life insurer accounts for the fact that they have received premiums, but the policy coverage extends into the future. Each of the three approaches—the General Measurement Model (GMM), the Premium Allocation Approach (PAA) and the Variable Fee Approach (VFA)—are used for different types of products. And, in the case of life insurance organizations, are used to guide how companies will deal with disclosure of Liability for Remaining Coverage (LRC).



Policy data will need to be analyzed carefully to allow the company to make reasonable judgement calls on which model to use. And that means that all data must be accessible, readable and standardized into a format suitable for performing the needed analysis.

Not something all insurance companies, especially those saddled with multiple legacy systems, are easily capable of.

## What are the challenges with each measurement approach?

Each of the three different measurement approaches present their own challenges.

### 1. GMM – General Measurement Model

The General Measurement Model is the default approach that any insurance company can use. It's appropriate for longer-term contracts like Life Insurance or Mortgage policies, which cover a specified risk over an extended period.



#### Challenges:

The main issue companies face when using GMM, is making the calculation of the time value of money on all cashflows and then applying risk adjustments. Most insurers are beginning to use GMM models but have limited prior experience working with similar models—which creates challenges around determining how to work with the necessary data.

### 2. PAA – Premium Allocation Approach

The Premium Allocation Approach is a more simplified approach than GMM. It can be used for short-term contracts—those providing less than 1-year of coverage. Complexity can result from this approach, because it can also be used for very specific longer-than-a-year contracts if the insurer can show that PAA and GMM approaches deliver comparable results.



#### Challenges:

Proving that the results from the PAA model and GMM models are similar is also a data challenge. Data must be accumulated, and analysis performed, to show, conclusively, that the derived outcomes of using one model versus the other are the same.

### 3. VFA — Variable Fee Approach

The third approach is called the Variable Fee Approach and is always required for “Direct Participating Contracts”. This measurement approach is mandated for contracts involving segregated funds, unit linked contracts, etc. and can be used for any insurance contract that involves investment components.



#### **Challenges:**

In the VFA model, the same data challenges faced when using the GMM apply, but, additional data and calculations are needed to figure the roll-forward handling of the Contractual Service Margin. In short—more calculations mean more data headaches for those lacking the right data processing tools and procedures.

**“ One of the biggest IFRS 17 challenges for insurance companies is that no matter which of the three methods you choose, the preciseness of the calculations in the measurement approaches is dependent on the accuracy and reliability of the underlying data. ”**

## Data defines how contracts are grouped

Data also poses problems when determining what level of aggregation to use for groups and cohorts. Different ways of grouping the contracts might generate distinctly different results, and companies need to identify which aggregation approach is most appropriate for their business. Again—insurers need data to make and support those decisions.

## Inefficient data processes create costly inefficiency

Further, without the use of right toolsets, insurers run the risk of creating inefficiencies in their data collation and analysis processes. Slower processes and increased manual effort mean more time and work required to generate compliance reports.



Those inefficiencies result, not just in higher costs, but also reduce the amount of time highly skilled employees are able to devote to tasks that generate much more value.

## **Succeeding & Surpassing IFRS 17 Standards – The IFRS 17 Modeling Solution**

IFRS 17 provides for flexibility in choosing which method to employ to measure policy liabilities. But choosing the best approach is a data-driven challenge. And that means, insurance companies need to be able to access all the relevant policy information across core insurance, accounting and actuarial systems.

That data must be converted so that it is searchable and relevant values can be extracted for use in analysis. Without automated data processes to enable this work, IFRS compliance will require more effort and create a drag on business-as-usual processes.

**Critical Challenge #3**

# Going Beyond IFRS 17 Compliance



## Getting a handle on IFRS 17 reporting

IFRS 17 will completely redefine the reporting requirements for insurance companies on its inception as early as January 01, 2023. In an effort to increase transparency and standardize reporting, the International Accounting Standards Board (IASB) has created a far-reaching new set of standards that affect everything from disclosures, to how profit and expenses are recognized, to how liability is measured for different policy types.

Given the scope of the changes required by the new standards, it's not surprising that many of the reporting directives have altered or are altogether new—so, the process by which companies get from source data to final reports has become very complicated.

**“ If an organization is not being able to effectively create and manage this process, that company will find itself non-compliant. The risk of hefty fines or interruptions to business, are too high to contemplate. ”**

## Changes to reporting requirements under IFRS 17

The new IASB standards are an attempt to go beyond offering just reporting instructions, and instead require companies to communicate the assumptions and information that went into their reporting.

These standards are meant to create greater levels of transparency than exist today—making it easier for all stakeholders to understand a company’s financials and to be able to compare them fairly against other insurers.

**“ This transparency is a noble goal—but it does bring with it a new level of complexity that is a challenge for most companies to address. IFRS 17 requires the creation of ten new and different types of disclosure reports. ”**

These new reports cover areas like reconciliation of insurance contract liabilities, eligibility for application for PAA and analysis of insurance revenue. They require explanations of income or expenses, recognition of the CSM, composition of components of the VFA, and how measurement of groups will be handled.

Even the presentation of the income statement is necessarily different from the IFRS 4 in significant ways. The new standard redefines how to calculate and report items like:

- ▶ Insurance revenue
- ▶ Incurred claims and expenses
- ▶ Insurance service result
- ▶ Insurance finance expense
- ▶ Net financial result

## IFRS 17 reporting challenges

These new reporting requirements create challenges because companies need to be able to access all their data at a new, deeper level of granularity that can provide them with the raw material for making new calculations and generating disclosures.

As well, in line with the IASB's desire to create transparency, companies need to be able to relate data and the assumptions that went into the calculations.

**In effect, they have to 'show their work.' And, that means being able to execute on three key steps:**

- ▶ Step 1: Define the precise calculations required for each report
- ▶ Step 2: Process the calculations in the right order
- ▶ Step 3: Identify the correct interpretation of each disclosure and generate them in the correct format

Standard Commercial-off-the-Shelf (COTS) platforms can make this implementation process easier. They already contain predefined calculations and report generation modules, which have been designed based on learning from the top accounting firms who regularly work with IFRS standards.

For most companies, making use of purpose-built software, as well as building strong partnerships with integrators, implementation vendors, accounting firms and consultants, will be the easiest and most effective method of achieving overall IFRS 17 compliance.

# A final word on IFRS 17

## Benefits of enhanced reporting beyond compliance

Although the data, modelling and reporting challenges involved in achieving IFRS 17 compliance are significant, the work done in order to prepare for the new standards can also create significant opportunities for insurers.

Better access to more data, and the ability to present it to all stakeholders in consistent and standardized ways, will not just enable companies to avoid the hefty penalties resulting from non-compliance, but will greatly enhance the organization's ability to treat data as a valuable strategic asset.

### Some of the many benefits of improved data management and enhanced IFRS 17 reporting include:

- ▶ Data transparency and shareability will heighten collaboration and improve decision-making across departments
- ▶ Improved access to data in real time will reveal new opportunities for everything from building more profitable products to enhancing customer experience
- ▶ Once the heavy lifting for IFRS 17 is done, the groundwork will have been laid to make compliance with future regulatory changes easier
- ▶ Better understanding of the metrics involved in the performance of each product can lead to faster innovation in response to market changes

# Achieving and Surpassing IFRS 17 Compliance

## Considering core system modernization

Beyond the reporting benefits, creating the entire IFRS 17 solution may push some companies into making larger, more strategic changes that will have positive impacts in the years to come.

For instance, IFRS 17 may be the tipping point that causes an organization to undergo a larger core systems modernization project. The effort involved in becoming IFRS compliant is large and costly. Other regulations will undoubtedly follow.

So, it makes sense to begin a modernization project now, so that the insurer becomes not just IFRS 17 compliant but enjoys all the other benefits of a modern rules-based policy administration system—like accelerated speed to market and increased operational efficiency.

Though there may not be enough time to fully modernize your core systems before the IFRS 17 deadline arrives—work on solving the data challenges and organizing to make the best use of new reports and business intelligence can begin today.

At the same time, work can begin on creating a roadmap for modernization and sunseting legacy systems—enabling forward-thinking companies to gain competitive advantage in the evolving insurance marketplace.

To continue the conversation about IFRS 17 and how Equisoft can help, feel free to connect with us.

## Contact our Insurance Solutions team

Find out how we can help you implement an award-winning IFRS 17 solution:

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