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Transcending the technical: the real business impacts of IFRS 17

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As insurers prepare for IFRS 17, some are starting to recognize that the new accounting standards will have a significant impact across many areas of their business.

By now, most insurers should already be thinking about the practical implementation of IFRS 17. Accounting and actuarial teams have read the new rules, begun estimating the financial impacts and started creating their roadmap to achieve compliance.

Insurers know that the shift to IFRS 17 will mean developing new accounting and actuarial policies and procedures and redesigned year end reporting process, documentation and controls. They recognize that the new standards will require designing systems changes to perform new calculations, the collection and storage of new data and rigorous testing to ensure smooth adoption. For those that have completed an initial impact assessment, activity has started to pick up pace at an operational level. Many of these front-runners are deep in the tactical steps needed in order to be able to dry run results on the new basis ahead of achieving compliance by 2021 — analyzing which of the available options is preferable in their particular circumstances, exploring how to mitigate volatility, working out how best to operationalize the requirements, probing matters of interpretation, and strategizing how best to use this opportunity to automate, streamline and standardize. Their executive teams have likely started to ask detailed questions about performance metrics and key performance indicators (KPIs) under the new standard.

Seeing the bigger picture

Yet, as management starts to dig deeper into the financial and operational impacts of IFRS 17, many are starting to uncover some unexpectedly wide business impacts and this is creating some concern in the executive suite.

For undertakings within the European Union, IFRS 17 will have no direct impact on prudential capital. But for other companies one of the most acute concerns we are finding relates to the potential impact of IFRS 17 on future available capital. Depending on the linkage between local financial reporting and prudential regulation in particular jurisdictions the new standards could, in some cases, alter the available capital which, in turn, impacts the amount of free capital that is available to support new growth opportunities, payment of dividends and to conduct M&A. Those with an eye towards their long-term growth strategy are understandably concerned and are looking to factor IFRS 17 metrics into their business planning.

It's not just those with ambitious growth plans and those that report their group results using IFRS that are taking a second and third look. Those with a global or multi-jurisdictional footprint are also concerned about how the shift to IFRS 17 will impact the dividend paying ability of their subsidiary operations. Planning future dividend flows and factoring this into the group's dividend policy and communicating this to investors will all be important — and require robust numbers ahead of time.

KPMG professionals have found that for some, the prohibition on recognizing 'day one' gains and the need to recognize losses on groups of onerous contracts will likely

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trigger important changes in product design and marketing. While the total level of profit will not change, the timing of its recognition will. This will be most significant for life insurers writing long-term business, where front end loading of profit is commonplace. Already, some insurers are exploring how they might pivot their focus away from day one profits — and that has the potential to benefit consumers as well as quality of earnings.

In matters of valuation there is no absolute truth, only perception. We believe the shift to IFRS 17 will impact the perceptions of shareholders, analysts and regulators — hence has the potential to impact valuation multiples and the value of any new acquisitions. Those embarking on inorganic growth or those considering the potential sale of books of business will certainly want to understand how the new standards may influence longer-term valuations.

CEOs and executives should also have a personal interest in the impacts of IFRS 17. Most are tied into performance-based bonus arrangements that are informed by finance KPIs. Many are justifiably worried as the new standards will change a variety of performance measures, specifically those using existing accounting bases, such as their remuneration packages. Those who have started exploring the presentation of their financials on the new basis will understand the major task required to educate the business in how to explain, interpret and, indeed, steer results on the new basis.

Breaking down the problem

If these issues have been weighing on your mind, and even if some of these issues haven't yet raised their heads, don't panic. There is still time to turn IFRS 17 business issues into competitive advantage. But the key is to be proactive.

For those organizations yet to start thinking strategically about the business impacts of IFRS 17, here are five steps you may want to consider:

1. **Create a cross-functional view.** Bring the directly impacted functions of accounting and actuarial and IT together with functions such as operations, marketing, distribution, product development and strategy, to create a holistic view of the potential impacts and strategies. Likely the effort will be led by the CFO and / or Chief Actuary, but the CEO and the Board need to be informed.

2. **Understand the implications.** Work within the functions to assess how the business impacts will influence current and future operating and business models. Consider what you might want to change in order to respond to these impacts and how these can be used to create competitive advantage.

3. **Assess the impact for local reporting and the impact for capital and dividend paying capacity.** Explore your various potential scenarios under IFRS 17 and consider how these scenarios may impact your capital ratios. Over time, reassess the scenarios to reflect new information and interpretations or changes in your marketplace.

4. **Cross check against your future strategy.** As the implications — both financial and operational — come into view, take the time to reassess your current and long-term business strategies and models to ensure these are being presented in their best light in the new world of IFRS 17.

5. **Talk to your stakeholders.** Once you understand how IFRS 17 will impact how you communicate your financials, spend time to talk to your key stakeholders — first internally in the business and then investors, regulators, brokers, reinsurers, agent networks and employees — to help manage expectations and ensure the right story is being communicated.

KPMG professionals' experience since the issue of the standard in May suggests that one of the biggest risks related to IFRS 17 is that executives view it as a purely technical initiative owned by accounting and actuarial. Indeed, with major business impacts looming, those who are not planning ahead and thinking about the impacts of IFRS 17 may find themselves veering off plan. Or, in extreme circumstances, unable to meet commitments to shareholders, regulators and even customers.

Those thinking strategically about the business implications of IFRS 17 today should be the ones who are best placed to navigate the business impacts of the transition to the new standard in 2021. ■

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