

New insurance accounting standard brings greater comparability for investors and analysts: KPMG

The new insurance contracts accounting standard published today by the International Accounting Standards Board (IASB) brings greater comparability for investors and analysts, according to KPMG International

- *Increased transparency about profitability expected*
- *Potential for greater volatility of insurers' financial results and equity*
- *Major implementation effort needed*

KPMG International welcomes the publication today of the new, long-awaited accounting standard for insurance contracts, IFRS 17. This new, comprehensive accounting model is 20 years in the making and heralds an end to the lack of comparability in the insurance sector.

Due to take effect on 1 January 2021, the new standard is the result of years of discussion, exposure drafts and debate. Although it has long been recognized that current accounting practice did not offer sufficient comparability between the financial positions and performance of insurers in different jurisdictions and with companies in other industries, the complexity of insurance accounting and variety of products meant that agreeing on a new standard was an extremely challenging task.

“We welcome the new standard and congratulate the IASB on this significant milestone after years of endeavor,” said **Gary Reader**, KPMG’s Global Head of Insurance and a partner with KPMG in the UK. “The greater comparability and greater transparency that IFRS 17 provides should be a clear benefit to analysts and users of financial information.

“For the first time, insurers will be on a level footing internationally. It will open up the ‘black box’ of current insurance accounting. However, these and other potential benefits will only come through the hard work of implementing the new standard, which we expect will raise several challenges for the sector. It will be a tough task for many.”

Key effects of the new standard

The new standard will give users of financial statements a whole new perspective. The ways in which analysts interpret and compare companies internationally will change. Increased transparency about the profitability of new and in-force business will give users more insight into an insurer’s financial health than ever before.

- Separate presentation of underwriting and finance results will provide added transparency about the sources of profits and quality of earnings.
- Premium volumes will no longer drive the ‘top line’ as investment components and cash received are no longer considered to be revenue.
- Accounting for options and guarantees will be more consistent and transparent.

These have the potential to reduce the cost of capital for leading insurers. Greater comparability could facilitate merger and acquisition activity, encourage greater competition for investment capital and help gain the trust of investors.

At the same time, there are likely to be a number of other effects. For example, there could be greater volatility in financial results and equity due to the use of current market discount rates.

Insurers may also need to revisit the design of their products and other strategic decisions, such as investment allocation.

Impact on insurers will vary widely

The impact of the new standard will vary significantly between insurance companies.

Mr Frank Dubois, Insurance and Actuarial Advisory Partner at KPMG in Singapore commented: “Insurers will have to consider how the new standard will impact their regulatory reporting as well as Group reporting, if not based on IFRS. With no indication from regulators to converge regulatory reporting requirements to IFRS 17, insurers may potentially be required to maintain at least two sets of financial numbers and reconciling them will be a complex process.

It is important for insurers to comprehend the differences under all reporting requirements to have an overall view of the implication and effort required locally. An early understanding of these impact is essential to managing the implementation journey.”

Implementation challenges

The implementation date of 1 January 2021 may seem a long way off – but the timescale will be a challenge for many.

Implementing the new standard will require substantial effort, and new or upgraded systems, processes and controls. This task will be even more challenging given the long time horizons over which many insurance companies operate and the legacy systems that many still use.

Mary Trussell, KPMG’s Global Insurance Accounting Change Leader and a partner with KPMG in Canada, commented: “For most insurers, adopting the new standard will have a bigger impact and be a greater challenge than adopting IFRS in the first place. The journey isn’t over yet. The new standard will trigger a second wave of activity by local accounting and actuarial bodies, tax authorities and prudential regulators – everyone will want to know how the new accounting requirements will interact with capital requirements.

“A coordinated response will be essential. Finance, Actuarial and IT functions will need to work closely together like never before. The time to watch and wait is over – the need for planning starts now.

“Forward-looking insurance groups have already started analyzing what the changes mean for them – don’t underestimate the need to evaluate and test new systems and processes, and educate business users and investors. In general, the more jurisdictions an insurer operates in and the more products it offers, the more costly and time consuming implementation will be – but so too is the potential to benefit from the changes.

The more I work with insurers on implementation, the more I see them saying: ‘Why do we do things the way we do? Why don’t we set up centers of competence instead of duplicating activities 20 times over?’ Faced with a change of this magnitude, it becomes a much easier decision to invest to achieve efficiencies. Absent this change, you’d just live with a status quo. For the confident, change is opportunity.”

Note to editors:

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Twitter: @KPMGSingapore

For further information, please contact:

Yasmin Quek
External Communications
Tel: +6507 1546
Email: yquek@kpmg.com.sg

Kelvin Lee
External Communications
Tel: +65 6507 1534
Email: kelvinlee1@kpmg.com.sg