Love it or loathe it, IFRS 17 is on its way

Understanding the new reporting standard for insurance contracts

Stephen Makin,
Partner, Head of Life & Financial Services, Scotland

Andrew Scott
Senior Consulting Actuary

Elaine Murphy
Senior Consulting Actuary

Yaryee Wong
Consulting Actuary

20 July 2017

HYMANS ROBERTSON

Agenda

- Overview of standard
- Calibration and ALM implications
- Product development and reinsurance
- Q&A

Overview of measurement

Measurement model	Criteria	Example
Building Block Approach (BBA)	• Cash flows are independent of underlying investment strategy	• Conventional non-profit annuities • Protection business
Variable Fee Approach (VFA)	• Clear pool of underlying items • Substantial portion of cash flows vary with underlying items • Policyholders receive a substantial share of the returns	• Conventional and unitised with-profit contracts • Unit-linked contracts
Premium Allocation Approach (PAA)	• Short duration • No embedded options / guarantees • Measurement is a good approximation to the BBA	• Reinsurance contracts held • General insurance contracts • Group protection contracts

Liability components

1

Future cash flows

- Claims, benefits, premiums and expenses estimated using up-to-date information
- VFA: projected assets less charges plus cost of guarantees

2

Discounting

- Market consistent interest rate
- Top down or bottom up approach
- Assets need not be held

3

Risk adjustment

- An assessment of the future uncertainty of amount of future cash flows
- Similarities to the Solvency II risk margin

4

Contractual Service Margin

- Represents the unearned profit of an insurance contract
- A liability held on the balance sheet

Comparison of the CSM

4 Contractual Service Margin

Assumption	Building Block Approach	Variable Fee Approach
Changes in past claims / claims incurred	CSM **not** recalculated. Impact flows through to P&L	
Changes in non-financial assumptions impacting future cash flows	CSM recalculated to reflect the impact on the change in profit	
Changes in financial assumptions, such as interest rates	CSM **not** recalculated. Impact feeds through to P&L or OCI	CSM recalculated as interest rate changes affect the cash flow projection

Initial measurement - Example

Discount rate
5%

Risk adjustment measured using cost of capital method

Acquisition costs
£100

Premium
£2,600

	1	2	3	4
Best estimate CFs	1,000	800	400	100
CoC	100	70	30	10

BEL:	£2,106
Risk Adjustment:	£193
Acquisition costs:	£100
Total:	£2,399
Premium:	(£2,600)

CSM: £201

Subsequent measurement - Example

	1	2	3	4	PV at t=1
Best estimate CF	1,000	800	400	100	1,211
Updated BE CFs	1,000	850	450	150	1,347

CSM at t=0

£201

CSM at end of t=1:

£75 - £19 = £56

Interest added	£10	£201 x 5%
Impact of assumption changes:	(£136)	(1,347 – 1,211)
Value of CSM before allocating to period:	£75	201 + 10 - 136
Allocation of CSM to current period:	(£19)	(75 / 4)

Transition

- Need to create an IFRS17 balance sheet for business already on the books
- Items relating to the current standard will disappear (e.g. DAC)
- CSM will have regard to conditions at inception
- If full retrospective approach unpractical:
  - “Modified retrospective approach”
  - “Fair value approach”

ALM considerations

IFRS 17

Solvency II

Diagrams are not to scale

Product development

Economics of products is not changing

Aggregation of contracts will drive profit signatures

- Greater transparency of loss-making contracts may lead to pressure on pricing teams

Gender-neutral pricing

Reinsurance contracts reported as separate portfolios

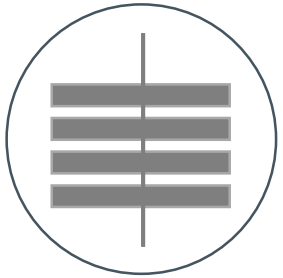
Other considerations

Making judgements in areas of discretion

Optimising impacts at transition

Developing new systems and processes

Educating and training stakeholders



Aligning remuneration packages

Questions

Contact details

Stephen Makin

stephen.makin@hymans.co.uk
0131 656 5164

Andy Scott

andrew.scott@hymans.co.uk
020 7082 6037

Yaryee Wong

yaryee.wong@hymans.co.uk
020 7082 6050

Elaine Murphy

elaine.murphy@hymans.co.uk
0131 656 5119

Confident

Partnering

Straightforward

Friendly

Thank you

HYMANS ROBERTSON