



Fluency in a brand-new financial language: how insurers are preparing to tell their story with the new IFRS 17 numbers

Foreword

Since 1 January 2023, International Financial Reporting Standard 17 (IFRS 17) has replaced the interim IFRS pronouncement that has been in force since 2005, IFRS 4. Because of that, it is natural to think that there is a way to link IFRS 17 back to IFRS 4. But that is not the case, given IFRS 4 was intentionally designed not to be a single accounting approach for all insurance contracts. It allowed application of accounting policies that varied significantly from company to company and was almost always supplemented by additional KPIs such as embedded value, Solvency II-linked items, or analysis of profits by source.

In this third article of a four-part series, we report on the views of the participants in the [2022 Global IFRS 17 Insurance Survey](#) on how they will use the new IFRS 17 financial language to communicate with investors. With the focus on building sub-ledgers, introducing new charts of accounts, preparing data, and updating actuarial

models, it is also sometimes easy with IFRS 17 to focus less on the numbers themselves, and the story they tell about the performance of the underlying business.

Yet, IFRS 17 is fundamentally different and indeed difficult to compare against IFRS 4, and “the numbers” are much more than just a new balance sheet and P&L with detailed disclosures. The survey shows that two aspects really stand out in terms of understanding the new world of IFRS 17:

- The mixture of economic measurement (for example through the best estimate liability and the risk adjustment) and the smoothed release of profits over a policy’s lifetime (via the contractual service margin, released through coverage units).
- The ongoing resetting each period of the insurance revenue to expected claims and expenses—

effectively a current “risk premium” measure that could make the comparison of revenue and profit margins between property & casualty (P&C) and life businesses more direct and understandable.

The Deloitte team observed that the analysts' feedback has so far been positive. Some positives have been called out after the initial IFRS 17 meetings with investors held by the large European insurers at the end of 2022, including comments on the reports being “more insightful,” “more stable,” better linked to underlying economics and even embedded value, and “reassuring.” As many of those whom Economist Impact interviewed attested, however, the range of key performance indicators (KPIs) will evolve over several years—hopefully building on this positive base.

Simon Walpole
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IFRS 17 changes financial reporting to such an extent that it can be compared to the arrival of a new language for insurance accounting—one in which insurers will need to become fluent. Along with new KPIs and performance metrics, insurers will use their IFRS 17 financial results to convey their performance to investors with the added aim to improve comparisons with peers. But how will the language of insurance accounting change, how easy will this new language be for stakeholders to understand, and what are the likely benefits?

Introduction

The introduction of IFRS 17 for insurance accounting is equivalent to the arrival of a new language. Insurers will have to learn it, change how they communicate to internal and external stakeholders, and become more fluent in telling the financial story of their business using this new reporting language. In part, this will need to be done through IFRS 17’s new metrics, which will enable insurers to use more granular data to reflect their performance more transparently and consistently with their peers—even as some legacy reporting figures will be discarded, raising difficulties for historical comparability.

The new standard could bring substantial improvements over IFRS 4 in terms of transparency and comparability. It would certainly bring an end to the protracted interim period when regulators accepted the loosely governed financial reporting

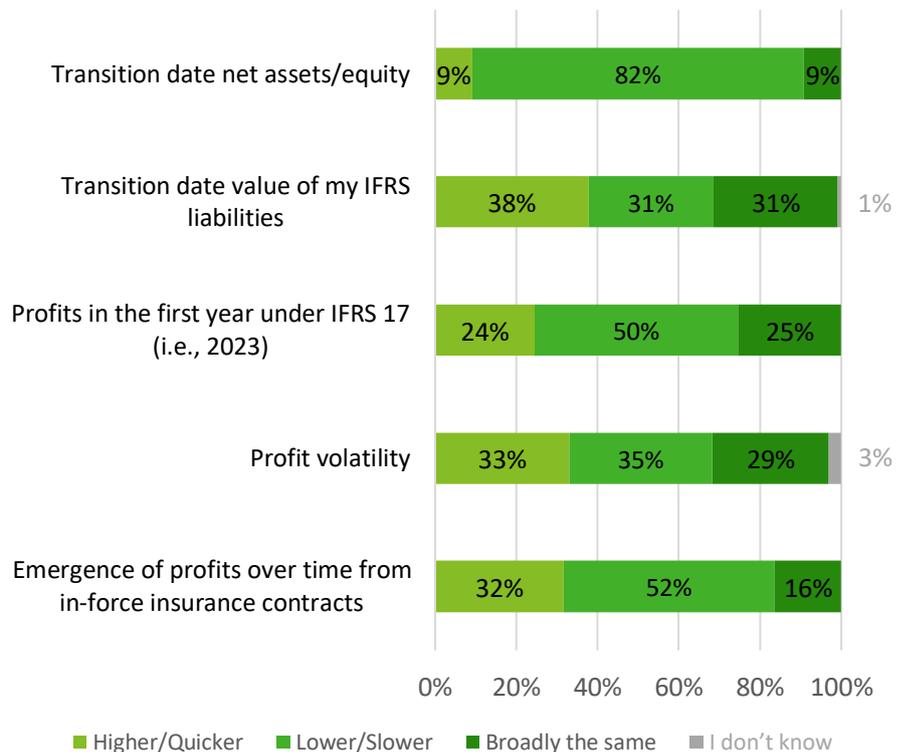
regime for insurance contracts, under IFRS 4 since 2005, in anticipation of having IFRS 17 ready to replace it.

When we asked firms what advantages they expect IFRS 17 to bring, survey respondents cited three principal gains: easier access to capital, improved operational efficiency in key functions, and financial statements that better reflect performance.¹

With such a radical change, financial metrics will inevitably be materially different. Most respondents expect that becoming IFRS 17-compliant will result in lower net assets/equity and—in the opinion of around half of the 360 executives surveyed—lower profits in the first year under IFRS 17 and the slower emergence of profits over time from in-force insurance contracts (see Figure 1), with the last particularly true for smaller firms as measured by net written premiums (NWP).



Figure 1: Please indicate the expected impact of compliance with IFRS 17 on your organization’s financial statements compared with current reporting requirements, following the transition date (i.e., 1 January 2022 for calendar year reporting entities adopting IFRS 17, with an effective date of 1 January 2023). Select one answer in each row.



Additionally, historical comparability might not be possible for years given that IFRS 17's new metrics will be published with only one year of restated comparative information. This will put insurers under pressure to convey the meaning and impact of these changes to their internal and external stakeholders. That means communication must be a core focus in the transition period and beyond.

Metrics and KPIs: Made to measure

The goal of IFRS 17 is improved transparency and consistency in financial reporting for entities that sell insurance contracts, and many believe the new standard will succeed in resolving some of the weaknesses of its predecessor: IFRS 4.

For Massimo Tosoni, Head of Group Accounting Policy & Reporting at Italy's Assicurazioni Generali SpA, and a member of the Financial Reporting Technical Expert Group of the European Financial Reporting Advisory Group (EFRAG), investors and analysts are expecting that IFRS 17 will overcome some of the problems inherent in IFRS 4.

"For example, [in IFRS 4] there is not an economic view, and investors like having an economic view of the business that is not obscured by cost accounting," he says. "Instead, we will have our best estimate, we'll have transparent indications which are around the risk margin and the contractual service margin."

Another weakness of IFRS 4, says Mr. Tosoni, was the time taken to recognize losses, particularly on life books exposed to guarantees with an ALM mismatch; IFRS 17's mark-to-market valuation will, he says, provide better evidence of such losses.

At the heart of this valuation approach are new metrics regarding risk, and how and when profit is taken from insurance contracts sold (see box). Given the breadth and complexity of the reform, it remains to be seen which of these analysts and investors will regard as the most significant KPIs, but executives who participated in the survey can already see that some will gain particular prominence.

The CSM and beyond

IFRS 17 contains numerous new metrics, with the contractual service margin (CSM) arguably the most significant. Briefly, the CSM spreads the expected profits on sold insurance contracts over the life of those contracts while recognizing losses immediately.²

The CSM applies to existing contracts and to new business and represents the unearned profit of the group of insurance contracts that the entity will recognize as it provides services in the future.³

Given the nature of insurance contracts, the CSM is a more complex requirement for insurers that issue coverage for longer than one year—for example, life firms.

Initial measurement

On initial recognition, the entity must measure a group of contracts at the total of the CSM and the amount of fulfilment cash flows (FCF). This measurement is at an amount that, unless the group of contracts is onerous, results in no income or expenses arising from:

- The initial recognition of an amount for the FCF: these are the estimated future cash flows adjusted to reflect the time value of money and the financial risks associated with those future cash flows, and further adjusted for non-financial risk.
- The derecognition at that date of any asset or liability recognized for acquisition cash flows.
- Any cash flows arising from the contracts in the group at that date.
- The liability for remaining coverage comprising the FCF related to future services and the CSM of the group at that date.
- The liability for incurred claims, comprising the FCF related to past service allocated to the group at that date.

In other words, when new business is written, assuming it is not onerous at the beginning, the future profit associated with that new business is deferred on the balance sheet, not resulting in an immediate profit or loss, along with an estimate of cash flows for that business.

Subsequent measurement

Subsequent measurement requires that the carrying amount of a group of insurance contracts at the end of each reporting period shall be the sum of:

IFRS 17 contains a range of other technical metrics on revenues, liabilities, risk, and discounting. Further detail is available in [this paper from Deloitte South Africa](#)—including the premium allocation approach (PAA), which simplifies how firms measure the liability for the remaining coverage on a group of contracts.



Ian Kelly, Group Chief Financial Officer at SCOR, a global reinsurer based in France, says the advent of IFRS 17 will see a shift in KPIs to measures of value creation—and, in particular, the new-business CSM, which “I feel will be a key metric upon which the market will anchor.”

“There will be a need to understand the level of value-creation that is coming from the new business that’s written, and then a level of value that emerges from the in-force business that people have on the books—how the CSM recycles into the equity of the group,” Mr. Kelly says. “I think that’s where some of the changes in KPIs will start to evolve.”

In the interim, he says, some in the market will likely revert to metrics used in regulations like Solvency II as they try to understand better those associated with IFRS 17. And, Mr. Kelly adds, “there will be quite some focus upon cash as the market attempts to get used to the new suite

of metrics.”

Roman Sauer, Allianz’s Head of Group Accounting and Reporting, views the CSM as the key KPI due to its effect on the P&L and the balance sheet. Indeed, he believes IFRS 17 will boost balance sheet visibility and generate more reliable ROE figures than in the past—and without firms needing to correct the accounting mismatches that came with adherence to IFRS 4.

“There will be more focus on the balance sheet—and not only on the equity, but also on the CSM, and then on the combination of equity and CSM—the kind of value development where you can read much more out of the balance sheet than in the past.”

17 will and will not change became more pressing given when this survey was done the implementation date was looming. Yet, when we asked executives how they felt their firm was doing on this, just one in ten “strongly agreed” that their directors, senior management, and investors had a good understanding of the implications of IFRS 17 for the firm as of June 2022 when our poll closed (see Figure 2). In 2018, by comparison, that proportion was around one-third.

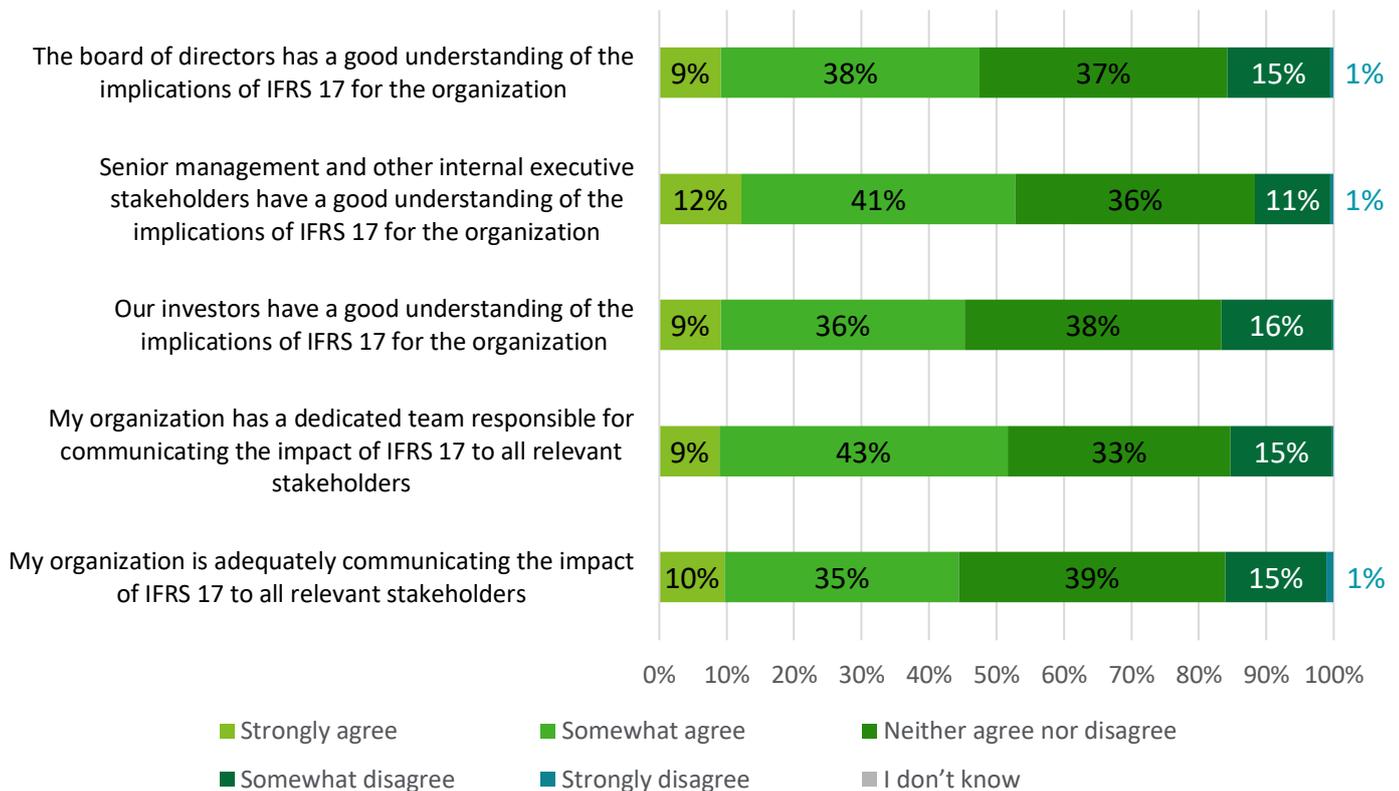
“There will be more focus on the balance sheet—and not only on the equity, but also on the CSM.”

Roman Sauer,
Head of Group Accounting and Reporting, Allianz

Communications 101: Preparing the internal audience

The need to communicate what IFRS

Figure 2: To what extent do you agree with the following statements regarding your organization’s level of communication on IFRS 17 to its stakeholders? Select one answer in each row.



“IFRS 17 features in nearly every discussion we have with our board and audit committee on financials—but we are no longer talking theory: we are talking numbers, which really helps... to start anchoring the new basis.”

Karthik Thilak,
Group Head of Financial Accounting and Reporting, Zurich



More positively, nearly 40 percent of respondents “somewhat agreed” that stakeholders had a good understanding of the implications of IFRS 17 for the firm, while most of the rest held a neutral view. Segmented by type of business, life firm respondents were much more likely to agree that their board (53 percent) and investors (52 percent) had a good understanding of the implications than non-life peers (42 percent and 39 percent respectively).

If nothing else, those results show there is room to improve. For Karthik Thilak, Group Head of Financial Accounting and Reporting at Zurich Insurance Group (Zurich), a steep learning curve for internal and external stakeholders is likely in the coming months “because [IFRS 17] is what we will have to live with.” The secret, he says, is “all about the power of repetition.”

“We see our teams already starting to think in IFRS 17 terms, and we do try to put them on the spot to say this is what it is—now, tell us what you understand and what you don’t,” Mr. Thilak says of Zurich’s approach to improving internal understanding. “IFRS 17 features in nearly every discussion we have with our board and audit committee on financials—but we are no longer talking theory: we are talking numbers, which really helps... to start anchoring the new basis.”

The ability to place real figures in front of stakeholders is something Allianz’s Roman Sauer agrees is key.

“Internally, we have one-to-one sessions with every board member and every business head here at the group center to explain their specific numbers—the old numbers and the new numbers [under IFRS 17],” Mr. Sauer says. “They need to understand the figures and why figures are changing and what is driving that, and you can only explain to them by having their figures in front of them.”

Communications 101: Preparing the external audience

While internal communications are crucial, it is essential that firms can explain IFRS 17 and its effects to the broader audience of analysts and investors. Given the breadth and complexity of the changes, firms have their work cut out for them.

“You have to keep your story clear and simple to the market,” says Redmond Murphy, SCOR’s Deputy Group Chief Financial Officer, “because there’s a risk that the message is lost with the complexity and with lots of new numbers—and the market saying, ‘We can’t actually tell what’s going on with your business’.”

Allianz’s Roman Sauer says the months in the run-up to publication of new figures are a crucial time, with the insurer’s finance team switching from implementation mode to communication mode. To that end, they will talk in the coming months to investors, analysts, journalists, and the public to educate them on IFRS 17.

“We want to keep the trust that people have in our numbers going into the new regime, and that’s why we need to invest the time sitting with them and explaining,” he says.

Zurich, Prudential, Generali, and SCOR are among the other major players interviewed for this article that are also conducting outreach through investor days, web seminars, and other activities. As our survey found, there is a clear need for such work: half of respondents said they experienced “moderate or great difficulty” preparing investor relations and financial communications for shareholders and markets (see Figure 3).

Figure 3: In getting your company ready for the "go-live" date of IFRS 17, please indicate the difficulty your organization has experienced (or continues to experience) in working to successfully complete each step? Select one answer in each row.

	Great difficulty	Moderate difficulty	Minimal difficulty	No difficulty	Don't know	Total
Establish a program management team	47	119	143	51	0	360
	13.1%	33.1%	39.7%	14.2%	0.0%	100.0%
Retrieve data necessary for IFRS 17 calculations and reporting	46	146	129	37	2	360
	12.8%	40.6%	35.8%	10.3%	0.6%	100.0%
Upgrade existing capabilities of IT systems or implement new systems to comply with the new IFRS 17 requirements	48	139	132	41	0	360
	13.3%	38.6%	36.7%	11.4%	0.0%	100.0%
Complete user acceptance testing of the new systems and processes	48	150	126	36	0	360
	13.3%	41.7%	35.0%	10.0%	0.0%	100.0%
Produce the opening balance sheet at transition date (1 January 2022)	56	152	123	29	0	360
	15.6%	42.2%	34.2%	8.1%	0.0%	100.0%
Produce "parallel run" IFRS 17 financial information during 2022	45	124	158	32	1	360
	12.5%	34.4%	43.9%	8.9%	0.3%	100.0%
Review the operating model of actuarial, regulatory reporting, finance, and risk functions	47	132	143	37	1	360
	13.1%	36.7%	39.7%	10.3%	0.3%	100.0%
Educate and train staff who have not been involved in the implementation of IFRS 17	47	147	123	43	0	360
	13.1%	40.8%	34.2%	11.9%	0.0%	100.0%
Prepare investor relations and financial communication for shareholders and markets	50	130	138	41	1	360
	13.9%	36.1%	38.3%	11.4%	0.3%	100.0%
Engagement with your organization's external auditors to audit IFRS 17	45	129	147	38	1	360
	12.5%	35.8%	40.8%	10.6%	0.3%	100.0%

It is not just for investors and analysts that communications are lacking; almost half of respondents said they had "great or moderate difficulty" engaging with their organization's external auditors to audit IFRS 17.

That chimes with the experience of SCOR's Ian Kelly, who says bringing stakeholders along on the process has been a significant challenge.

"A key element I would highlight is ensuring that the work that we still have ongoing with the auditors gets to the right place—and we're still in progress there, and that needs to be completed in the timeframe of the implementation and publication [of results] next year [2023]."

When it comes to analysts, Zurich's Karthik Thilak says the insurer will, among other steps, provide supplementary information to its

financial statements to ensure they can adjust their models based on the new data. Zurich also explained its targets based on the new standard to investors at its investor day in mid-November 2022.

"It's going to provide a goalpost for everyone to understand what it means—and I expect that it will trigger more conversations," he says of Zurich's approach to external stakeholders.

A slow road to consensus

James Turner, Group Chief Financial Officer at insurer Prudential plc, explains that while Prudential will be doing “lots of education, both internally and externally, to ensure people understand what’s going to happen in terms of the different types of business, the different types of product, and the impact of the accounting standard,” an equally important focus is what IFRS 17 will *not* affect.

“The key point is [IFRS 17] doesn’t change any of our underlying cash flows—our product cash flows. Therefore, although it is an important accounting change and one that brings changes in the timing of profit recognition, it doesn’t change the economics of the business.”

James Turner,
Group Chief Financial Officer,
Prudential plc

“The key point is it doesn’t change any of our underlying cash flows—our product cash flows,” Mr. Turner says. “Therefore, although it is an important accounting change and one that brings changes in the timing of profit recognition, it doesn’t change the economics of the business.”

“So, part of the education will also be highlighting that you can still judge us on the economic measures that guide us in how we run the business and allocate capital—and how those are comparable with where we’ve been in the past,” he says.

Looking ahead, Mr. Turner believes the lack of comparability will prove a tricky issue for the industry to navigate.

“Given where people have come from in terms of their grandfathered IFRS 4, the initial impact of moving to IFRS 17 for each insurer will be different. There also won’t be full comparability on historical business due to the various transition measures,” he says.

“We are seeing the impact of this as insurers start to educate the external market on how they view the standard—we can already see that there is not a one-size-fits-all approach to determining both the standard’s effect on equity or profit and the different outcomes for individual products, cohorts of business, and individual countries for each company,” says Mr. Turner. “This will initially make it difficult for external stakeholders to form expectations and understanding across the industry.”

On that issue of comparability, he adds, IFRS 17 “won’t provide all the information our investors need.”

“So, we’ll continue to report our economic profit,” he says. “And we’re going to continue the non-GAAP measures for operating profit, because IFRS 17 will not capture the information that our investors need to understand how our business is performing over the long-term.”

SCOR’s Redmond Murphy agrees that it will likely take a year or two before standard KPIs settle in and you see “some gravitation toward some norms.”

“Everybody’s coming at [IFRS 17] with a different perspective, and there hasn’t really been an agreement on what everyone’s going to do,” Mr. Murphy says. “For us, [IFRS 17] is a positive because we have a significant life business, and we can demonstrate that value more clearly. But others have different stories—so, I think the KPI issue will take a while to settle.”

Ultimately, given the breadth and complexity of the changes, it will take time for the market to fully understand and be able to compare companies on an IFRS 17 basis. The real test will be over time after IFRS 17 has come into force and new accounts are published such that a track record is established, says Prudential’s Mr. Turner.

“When the rubber hits the road and people see real numbers through periods of market volatility,” he says, “that’s when the real understanding and embedding of IFRS 17 will happen.”



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End notes

1. See also our second article in this series, on technology <https://www.deloitte.com/global/en/Industries/financial-services/perspectives/global-ifs17-insurance-survey.html>, for more on these benefits.
2. The IFRS 17 Contractual Service Margin: A Life Insurance Perspective, Institute and Faculty of Actuaries (2020). See: https://www.actuaries.org.uk/system/files/field/document/IFRS17_CSMWorkingParty_SessionalPaper_5Oct2020.pdf
3. IFRS 17 Insurance Contracts - Standard Summary (2017): <https://www2.deloitte.com/za/en/pages/financial-services/articles/summary-of-standard-ifs17.html>

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