IFRS 17 Implementation: Different Companies, Different Approaches

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Regulatory changes often represent significant challenges and efforts for the individual departments. IFRS 17, however, will not only affect one department, since it requires changes that involve almost every stakeholder, functional area, system, person and process. In the past, we have seen software providers offering end-to-end solutions to comply with regulatory changes. However, PwC observes very different approaches to implement IFRS 17 in our clients' projects. In this article, we will outline reasons that lead to this broad variation of strategies and present recommendations on how to successfully implement IFRS 17.

What are the challenges when implementing IFRS 17?

IFRS 17 will require companies to replace a wide range of different accounting practices and, therefore, they have to revise their underlying accounting systems. The operational impact is considerable: additional policy and insurance data will be needed, more cash flow information will have to be analyzed and new ways of presentation and disclosure will be required. The adoption needs significant planning in alignment with the individual environment of each insurance company.

In order to successfully plan the implementation, insurance companies have to perform an IFRS 17 impact assessment and understand the gaps between what they have and what they need. At this point, the companies start to struggle with how to jump from the gap assessment to the implementation over the next couple of years.

Designing new technical systems to integrate all of these changes is especially difficult due to legacy systems already in place. However, since system implementation is not the only key driver for change, transformation requires a dialogue between human and machines in the organization. This is not about one dictating terms to one another; they need to come together within a more collaborative organizational design.

Another challenge faced by the insurance companies is the technical interpretation of the new standard. Therefore, IASB established a working group (Transition Resource Group, TRG) to provide a public forum for stakeholders to follow the discussion of questions raised on the implementation of the new standard. The insurance TRG addresses unit of account, contract boundary, and coverage unit issues.

For many insurers, IFRS 17 will fundamentally change the way they manage, measure and report business results. Although the changes require a lot of effort from the whole company, this new standard gives the opportunity to revisit the business model and optimize the financial reporting infrastructure.

Compliance only vs. maximizing investment

The degree of modernization may vary significantly across different companies, from «compliance only» to «finance transformation». Insurers following the «compliance only» approach, set their focus on the investment requirements to comply with the regulatory change. Accordingly, companies keep existing ledgers, actuarial platforms and sometimes leverage investments in Solvency II. Given the existing timeframe to meet the IFRS 17 regulation, the reduced scope of transformation represents a more secure approach.

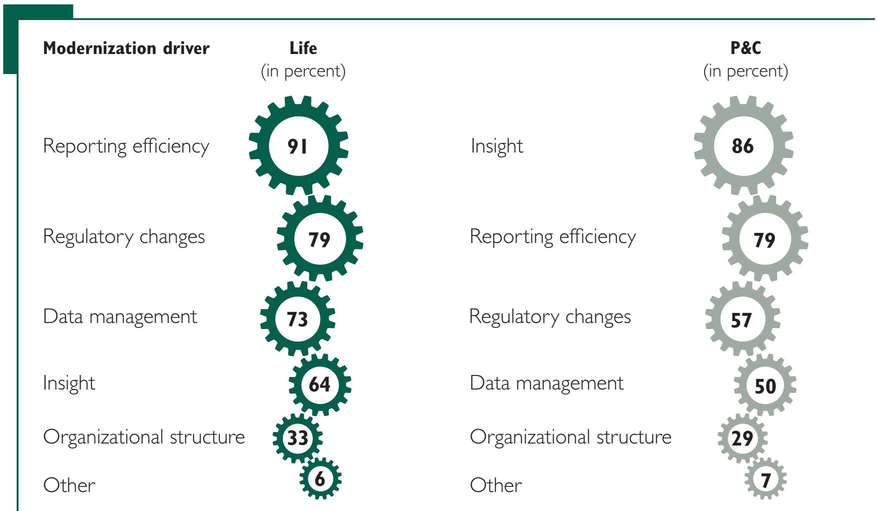

Figure 1: Drivers of modernization (PwC, 2018)

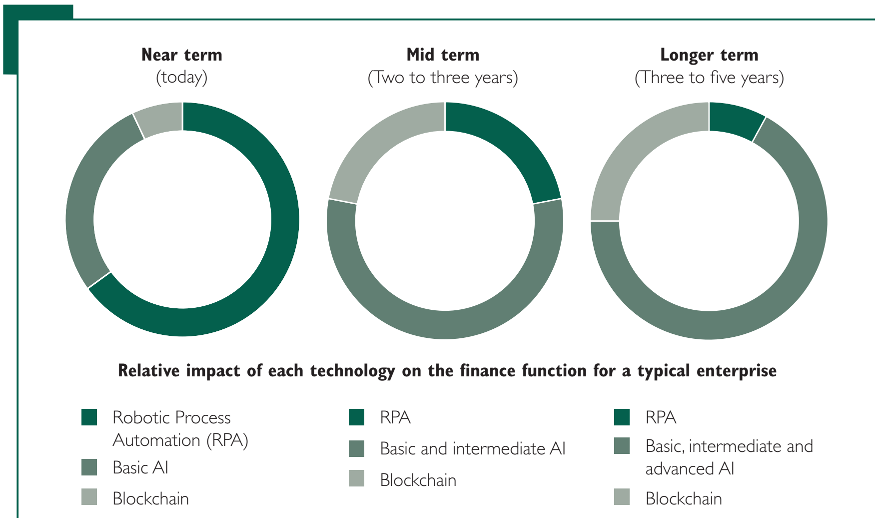

Figure 2: Which technologies will have the biggest impact on finance (PwC, 2018)

In contrast, those insurers who focus on finance modernization extend their budget and scope to actually improve performance, establish business intelligence tools, standardize systems and build end-to-end processes. The results of the Actuarial Modernization Survey 2018 conclude that regulatory changes are a main driver for modernization, apart from reporting efficiency and insight (Figure 1).

Aside from regulation, the implementation of IFRS 17 provides the «business case» to create an enhanced finance function, which delivers value and insight to business partners. The portfolio of new technologies and insightful tools is diverse. Possible technologies include virtualization applications, cloud high-performance computing capabilities and new analytical tools that leverage machine learning (Figure 2).

Additionally, the newly generated data could produce insights that provide innovative insurance companies a competitive advantage over the competitors who rely on customary processes and technologies. For example, the insights can be used in proactive risk management and may ultimately reduce the number of claims and lower expenses. Especially, the finance function presents a good opportunity for integrated management accounting by providing real-time data, claim assumptions and scenario analysis, which enables the user to be aware of the potential issues and opportunities earlier on. The future of finance requires a strategic modernization of finance, actuarial assumptions and risk into an integrated model. Therefore, the companies should integrate report and management information, share data, implement cloud-based finance applications and automate processes to lead and keep the transformation process.

Another benefit of modernization is the reduction of costs achievable with a change to a cloud solution which is more flexible regarding the pricing and capacity, or the replacement of legacy systems, saving high maintenance costs. In the end, the optimal approach to tackle the IFRS 17 transformation strongly depends on the time limitation and the long-term finance strategy of the company.

Complexity resulting in different sourcing strategies

Whom can you team up with in such highly complex transformation projects? As technology is a cornerstone for all IFRS 17 transformation processes, the sourcing strategy is a relevant success factor that needs to be considered. In the past, there were different end-to-end solutions, which guaranteed compliance with the regulatory standards. However, this is not the case for IFRS 17. During PwC's IFRS 17 Technology Showcase tour last year, the insurance company panelists discussed the topic of possible vendors. In line with our analysis, they agreed on the fact that a multi-vendor approach is necessary to cover the end-to-end requirements.

The big number of components and their inter-dependencies define the complexity of modernized architectures (Figure 3). In addition, the single components may influence processes, people as well as data control and thus need a considerate decision about whether to develop an in-house solu-

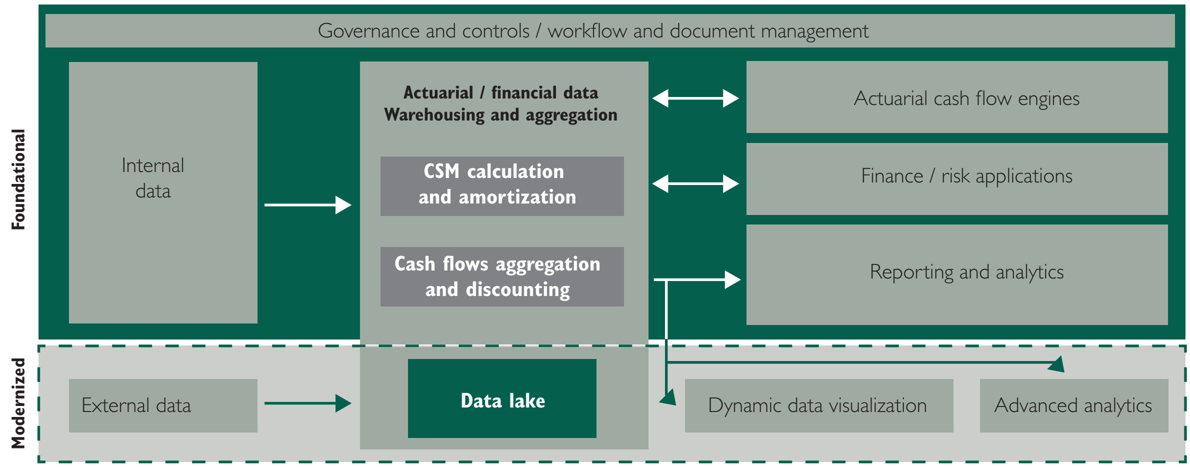

Figure 3: Illustrative modernization reference architecture (PwC, 2017)

tion or to purchase a solution outside of the company.

Unfortunately, many smart solutions offered on the market are currently not mature enough to integrate them. If companies hesitated to kick-off their implementation process until the finalization of the end-to-end architecture concept, they would very likely struggle to put all parts together in time. Therefore, many companies are using a soft design approach where one can tweak the details of the plan along the way.

Differing take-off points

Another major, investment-intensive regulatory change has been Solvency II, which came into force on 1 January 2016. As insurers prepared for Solvency II with IFRS 17 on the horizon, the implementation strategy already varied across companies six years ago.

Some of the costly investments in the IT architecture, like data warehouses, now turn out to not be compatible with new requirements and thus put more emphasis on a more flexible and forward-looking strategy. An example for beneficiaries from maximizing investment strategies is one of our clients who decided to migrate about 30 of its actuarial valuation systems on a single cloud-based actuarial platform with a data warehouse, automation, integration and workflow. Another example is the use of data lakes, which we identified as key component of a flexible, future-ready solution. Two of the many advantages of data lakes are the flexibility to save data in different formats and the timely availability of big volume data streams that is needed for advanced analytics. Thus, the computation of new key figures like the contractual service margin (CSM) or the integration of new applications, require significantly less effort for companies using data lakes than those using data warehouses.

For these forward-looking insurers, the implementation of IFRS 17 will be much simpler, as the advanced take-off point actually allows an easier and hence faster integration into the modernized system. Furthermore, they profit from the additional capacity to invest into solutions that may require more effort to develop and integrate and that have a better strategic fit.

Finally, companies lagging behind sometimes have to pay a mark-up for their bad take-off point, since some modernization initiatives are long lasting. Those changes then cannot be implemented within the timeframe of the IFRS 17 program, as another client experience highlights. The insurer wanted to replace its general ledger, including the migration of a high volume of data and the integration into a complex business environment. Due to the related delivery risk, the company decided to divide the project in two, a project fixing the current ledger and another for replacing the old one.

Learning from peers and prior experience

According to prior experiences, it is possible to conclude that there is no «one-size-fits-all» for IFRS 17 implementation. In fact, many companies are already implementing different approaches depending on their specific need. According to PwC's recent IFRS 17's impact assessment, peer companies are expecting the costs for IFRS 17 implementation to be between 80 percent and 500 percent of Solvency II costs depending on a number of criteria: level of investment in Solvency II in relation to process improvement, systems and standardization; availability of internal resource to support the IFRS 17 project; approach complexity regarding the CSM; degree of centralization and ability to manage large projects across complex groups; and leverage from IFRS 9. In order to determine a budget, it is crucial to establish the high, medium and low impact in the areas involved in the transformation. The effort will depend upon how many business units are in the scope of the gap analysis. Therefore, it is necessary to run an impact assessment to have a clear vision of the objectives for the IFRS 17 project and of the cost and effort required according to the company's needs, following standardized processes and learnings from prior experiences.

From our experience with Solvency II, we have learned three important lessons, which can be applied in the IFRS 17 transformation program:

- Leap forward with backward goal-setting
- Establish governance
- Assess what «good» looks like and be pragmatic.

Following a soft design approach has helped to establish the solution in time.

Conclusion

Regulatory changes have become a main driver for modernization of existing processes and are in the focus of senior managers. PwC observes various approaches on how to implement regulatory changes such as IFRS 17. The challenges are not only to fully understand and assess the impact those new regulations will have on the individual company, but rather to define a clear path for the environment of the insurance company with necessary steps. Legacy systems and the high complexity of necessary interaction between human and machine call for a more collaborative organizational design. We can see a trend across insurers that regulatory changes driven by modernization of tools and systems maximize their investments. As IFRS 17 is a highly complex transformation for any insurer, it is crucial to assess carefully whether to purchase an external solution or develop an in-house solution that covers all the components. Due to high interdependencies and complex architecture structure, insurers struggle to find solutions that fit all their needs. A common option for this problem is a soft design approach, which gives insurers a bit of flexibility when it comes to mapping out all the steps along their path. As other regulatory changes such as Solvency II came into force not so long ago, some companies have already taken up the challenge back then to do heavy investments in their IT architecture and implemented a more flexible, easier adaptable system. Especially data lakes have proven themselves as good fit for a constantly changing environment. As this is a modernization process that takes time, some insurers split their projects in two: one project for fixing the current ledger and another one for replacing legacy systems. As PwC has seen various approaches across the industry, there is not a «one-size-fits-all» solution. Many different variables play a role in implementing regulatory changes, but insurers can and have learned their lessons facing previous changes. Especially when it comes to planning such transformations, having a clear vision and standardized processes along the way can create a big impact on successfully implementing regulatory changes yet to come.

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