

SURVIVE THRIVE



Natural Selection

Financial Services Forum

21-22 May 2018 • Hilton Sydney



**Actuarial
Institute**



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Agenda

- Brendan Counsell – High level impacts of IFRS
- Siddharth Parameswaran – Sharemarket and analyst view
- Jennifer Lang – impact on managing the business



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Brendan Counsell

Partner, Ernst & Young

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Introduction

- IFRS 17 is a new international accounting standard for insurance contracts
- AASB 17 will replace AASB 4 and AASB 1038 from 1 Jan 2021
- IFRS 17 is expected to have wide impacts on profit reporting globally
- This presentation sets out some of the key changes under AASB 17 and discusses potential strategic implications for Australian life insurers













AASB 17 vs AASB 1038 – key changes

New requirement	Accounting implications
1. Lower level of grouping for liability measurement.	Profit recognition and loss components to be determined at a lower level.
2. Delineation between “liability for remaining coverage” (LRC) & “liability for incurred claims” (LIC).	Assumption changes affecting LIC will impact P&L in the period in which they occur.
3. Introduction of the “contract boundary” concept.	Limits cash flows included in liability measurement. Potential significant implications for stepped YRT.
4. Introduction of a “risk adjustment” (RA) for non-financial risk.	RA included as part of fulfilment cash flows and released over the coverage period.
5. Separation of reinsurance held from underlying direct contracts.	Reinsurance accounting may no longer align to that of underlying direct contracts.
6. Expense cash flows must be “directly attributable to the portfolio of insurance contracts”.	Some expenses may no longer be included as part of the liability measurement.
7. New measurement approach for direct participating contracts – the “variable fee approach”.	Significant change to liability measurement for participating contracts.

AASB 17 – an initial view of potential impacts

Key change	Key products affected	Opening net asset position	Future profit	Future profit volatility
1. Lower level of grouping	<ul style="list-style-type: none"> - Those with full retrospective approach on transition - All new business post transition 	<p style="text-align: center;"></p> <ul style="list-style-type: none"> - Higher liability due to less cross-subsidy between groups 	<ul style="list-style-type: none"> - Depends on business profile 	<p style="text-align: center;"></p> <ul style="list-style-type: none"> - Potentially more groups in loss, but lower \$ impacts
2. LRC and LIC.	<ul style="list-style-type: none"> - Income protection 	<p style="text-align: center;"></p>	<p style="text-align: center;"></p>	<p style="text-align: center;"></p> <ul style="list-style-type: none"> - Claim reserve assumptions to impact P&L.
3. Contract boundary	<ul style="list-style-type: none"> - Stepped YRT. 	<p style="text-align: center;"></p> <ul style="list-style-type: none"> - Higher liability due to DAC write off at transition 	<ul style="list-style-type: none"> - Depends on business profile - Potential higher ROE 	<p style="text-align: center;"></p> <ul style="list-style-type: none"> - Less sensitive to lapses & int rates, but depends on NB profile

AASB 17 – an initial view of potential impacts

Key change	Key products affected	Opening net asset position	Future profit	Future profit volatility
4. Risk adjustment	<ul style="list-style-type: none"> - Income protection - Group risk - i.e. large LIC 	 <ul style="list-style-type: none"> - Higher LIC - Higher LFC if in loss 	 <ul style="list-style-type: none"> - Depends on claims profile 	 <ul style="list-style-type: none"> - Magnifies LIC impacts
5. Reinsurance held	<ul style="list-style-type: none"> - All reinsurance contracts. 			
6. Directly attributable expenses	<ul style="list-style-type: none"> - Level term - Other long duration contracts 	 <ul style="list-style-type: none"> - Lower liability as may be lower allocated overheads 	 <ul style="list-style-type: none"> - Interpretation will affect materiality 	 <ul style="list-style-type: none"> - Interpretation will affect materiality
7. Variable fee approach	<ul style="list-style-type: none"> - Participating 			



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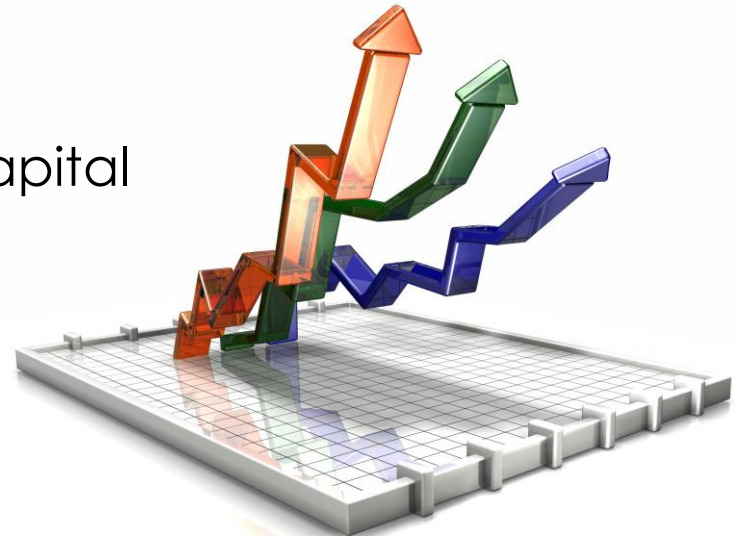
Jennifer Lang

CFO and Chief Actuary, CommInsure

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Managing the business

- How does profit measurement affect business management?
 - Key Performance Indicators
 - Management attention
 - Risk appetite outcomes
 - Measurement of economic capital
 - **Bonuses for executives**



Strategic implications of change

- Economics of business hasn't changed BUT
 - Reported profits are more volatile
 - Cross subsidisation no longer as hidden
 - Up front costs expensed at time of sale
 - Reinsurance and direct business not necessarily linked



Business changes that might emerge

- Retail business where DAC reduces:
 - Commission and upfront expenses managed more tightly
 - Loss making business clearer in short term results, hence action earlier
- Cross subsidisation between business lines visible
- Distinction between direct and overhead expenses
 - Expenses potentially more tightly managed
- Product changes optimising profit emergence

