

# Practical aspects of IFRS 17 (not only) in pension insurance

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13 June 2019

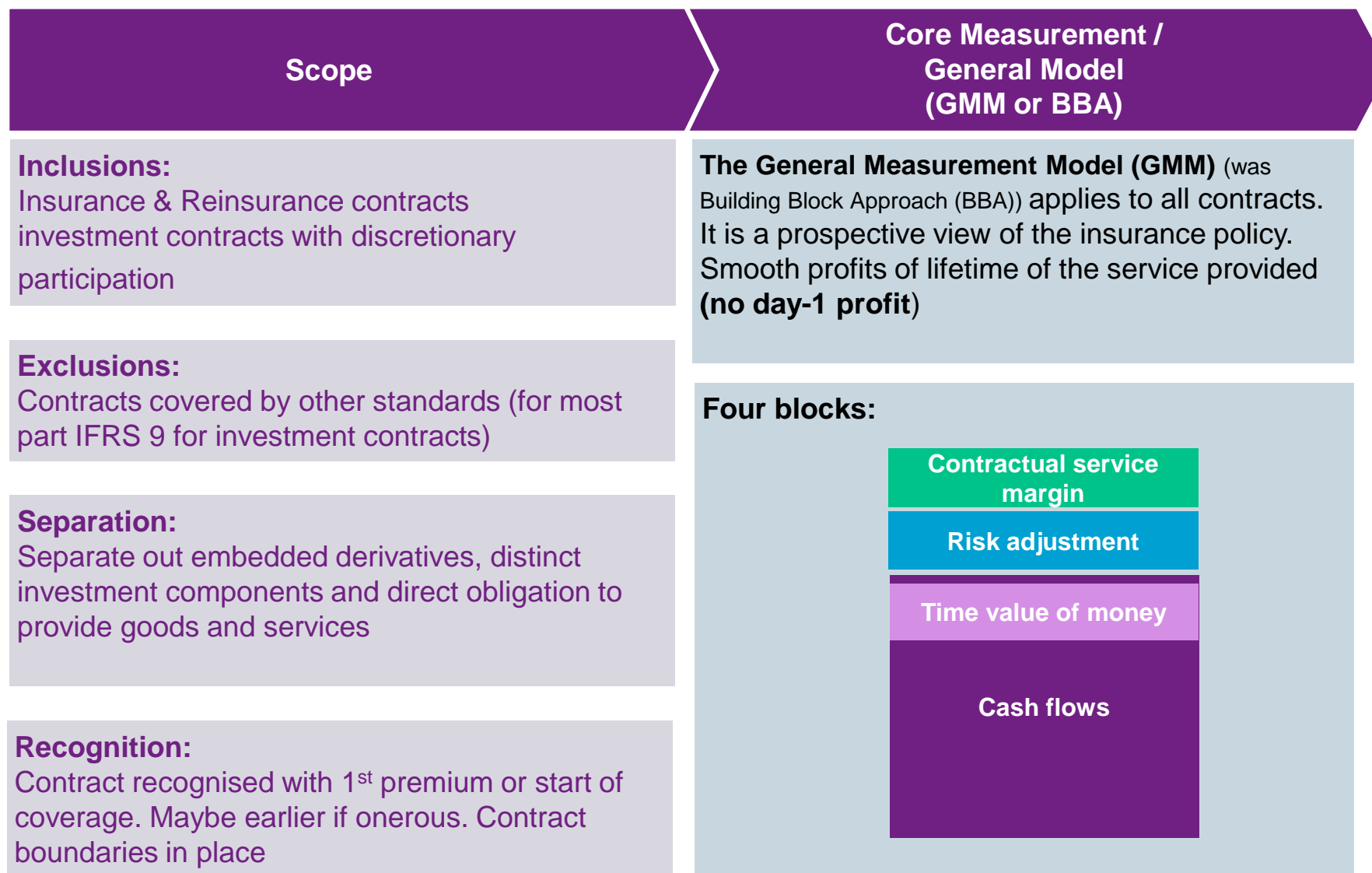


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# Overview of IFRS 17



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**Variable Fee Approach (VFA)** - modified approach for contracts with *direct participation features* (e.g. with profits)

**Premium Allocation Approach (PAA)** - simplified approach for contracts with <1year duration

For the **transitional period** where there is difficulty in applying a fully retrospective approach there is an option for a **Modified Retrospective Approach (MRA)** or if this is not possible a **Fair Value approach (FVA)** may be applied

## Coverage units

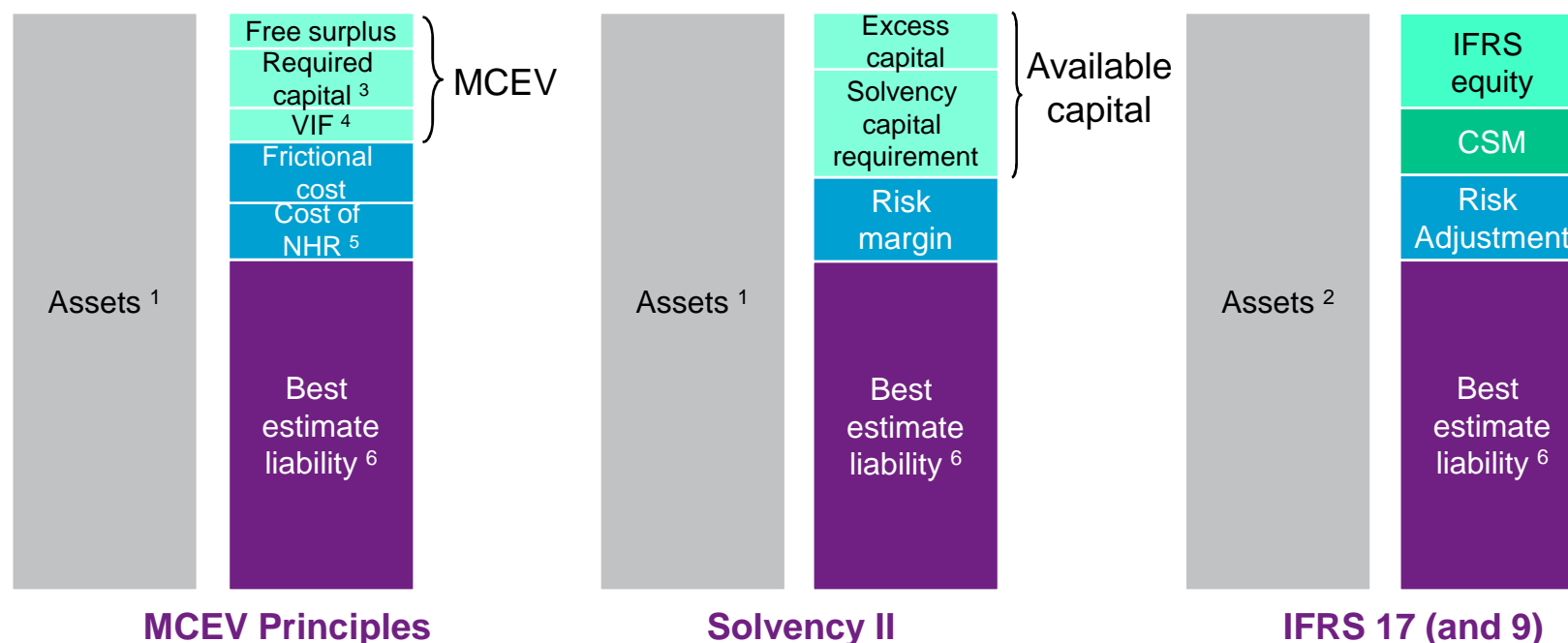


# Presentation

## Simplified balance sheet comparison

Presentation is more detailed and granular:

- Statement of financial position
- P&L
- Other comprehensive income
- Disclosures



<sup>1</sup> Assets measured at market value

<sup>3</sup> Required capital often is the greater of regulatory and internal capital

<sup>5</sup> Cost of residual non-hedgeable risks

<sup>2</sup> Assets measured at amortised cost or fair value, depending on asset type (IFRS 9)

<sup>4</sup> VIF after allowing for frictional cost and cost of non-hedgeable risks

<sup>6</sup> Best estimate liabilities might differ under the three approaches, e.g. discounting, contract boundaries

# Amendments to IFRS 17 considered by IASB: Overview of status

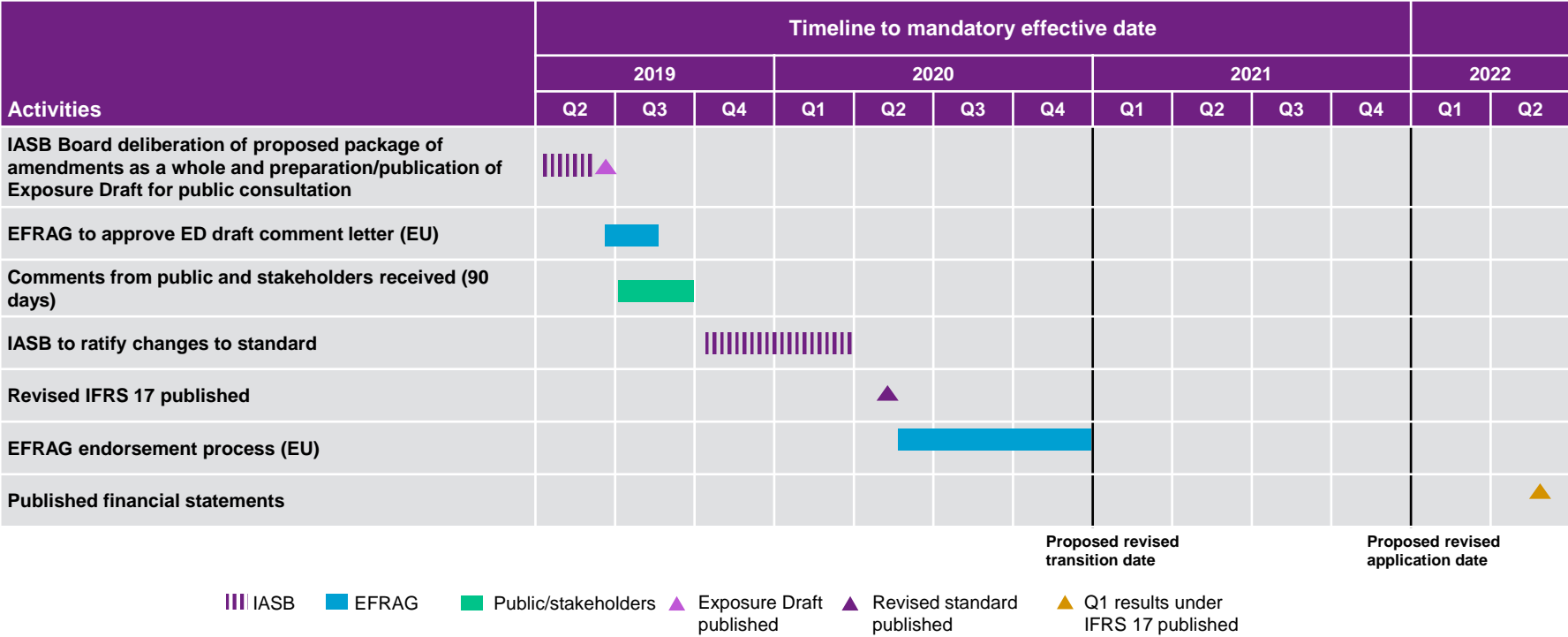
Tentative decisions by IASB; subject to review, balloting and ED

Date of initial application of IFRS 17	Temporary exemption from applying IFRS 9	Comparative information	Separate presentation of groups of assets and groups of liabilities	Presentation: Premiums receivable
Loans and other forms of credit that transfer insurance risk	Level of aggregation	Acquisition cash flows for renewals outside the contract boundary	Locked-in discount rates to adjust CSM	Subjectivity: Discount rates and risk adjustment
Risk adjustment in a group of entities	CSM: coverage units in GMM	CSM: limited applicability of risk mitigation exception	PAA: premiums received	Subjectivity: OCI option
Business combinations: classification of contracts	Business combinations: contracts acquired during the settlement period	RI contracts held: onerous underlying insurance contracts	RI contracts held: ineligibility for VFA	Subjectivity: Optional approaches on transition
Insurance contract with direct participation features	Interim financial statements- Treatment of estimates	RI contracts held: expected cash flows arising from underlying insurance contracts not yet issued	Modified retrospective approach: further modifications on transition	Fair value approach: OCI on related financial assets

Change(s) rejected
  Partial change proposed
  Change(s) proposed

# IFRS 17 proposed revised timeline

Final standard incorporating amendments expected Q2 2020



Sources: WTW interpretation of public comments made by IASB Board members; IASB staff papers; verbatim comments during IASB Board meetings; EFRAG 2019 work programme

## Pension insurance

Simple product

Savings part

- Regular paid premium (investment/savings amount)
- Premium invested into fund – guaranteed or non-guaranteed investment income
- At retirement age – lump sum or annuity chosen

Annuity part

- Lifetime annuity/ fixed period annuity
- Immediate/ deferred annuity
- Fixed/ variable
- Guaranteed

## Example

### Simple annuity

- Male, age 65
- Premium = 17 799.17
- Annuity = 1000
- Expense: fix = 90, initial\_fix = 625, variable = 1.5%

Age	Mortality rate	Survival rate	Policy cashflows		Company cashflows		
			Premium	Annuity payment	Fixed expenses	Initial expenses	Variable expenses
		1				625.00	
65.00	0.009784	0.990216	17 799.17	990.22	90.00		15.00
66.00	0.010708	0.979613		979.61	89.12		14.85
67.00	0.011791	0.968062		968.06	88.17		14.69
68.00	0.013057	0.955422		955.42	87.13		14.52
69.00	0.014533	0.941537		941.54	85.99		14.33
70.00	0.016248	0.926239		926.24	84.74		14.12
71.00	0.018235	0.909349		909.35	83.36		13.89
72.00	0.020531	0.890679		890.68	81.84		13.64
73.00	0.023176	0.870037		870.04	80.16		13.36
74.00	0.026214	0.84723		847.23	78.30		13.05



# Investment component

## What if we add

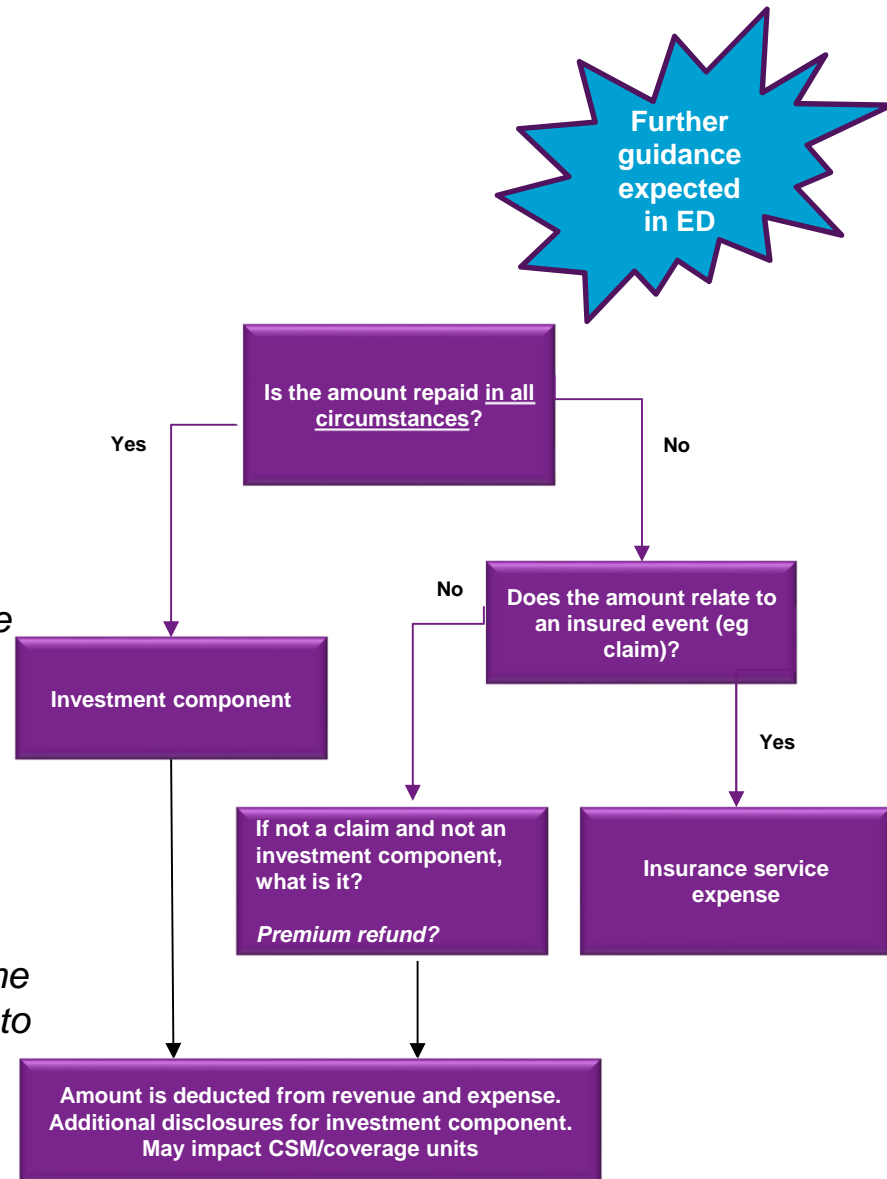
- guaranteed payment periods?
- deferral period with surrender options?

Appendix A of IFRS 17 defines an investment component as:

*“The amounts that an insurance contract requires the entity to repay to a policyholder even if an insured event does not occur.”*

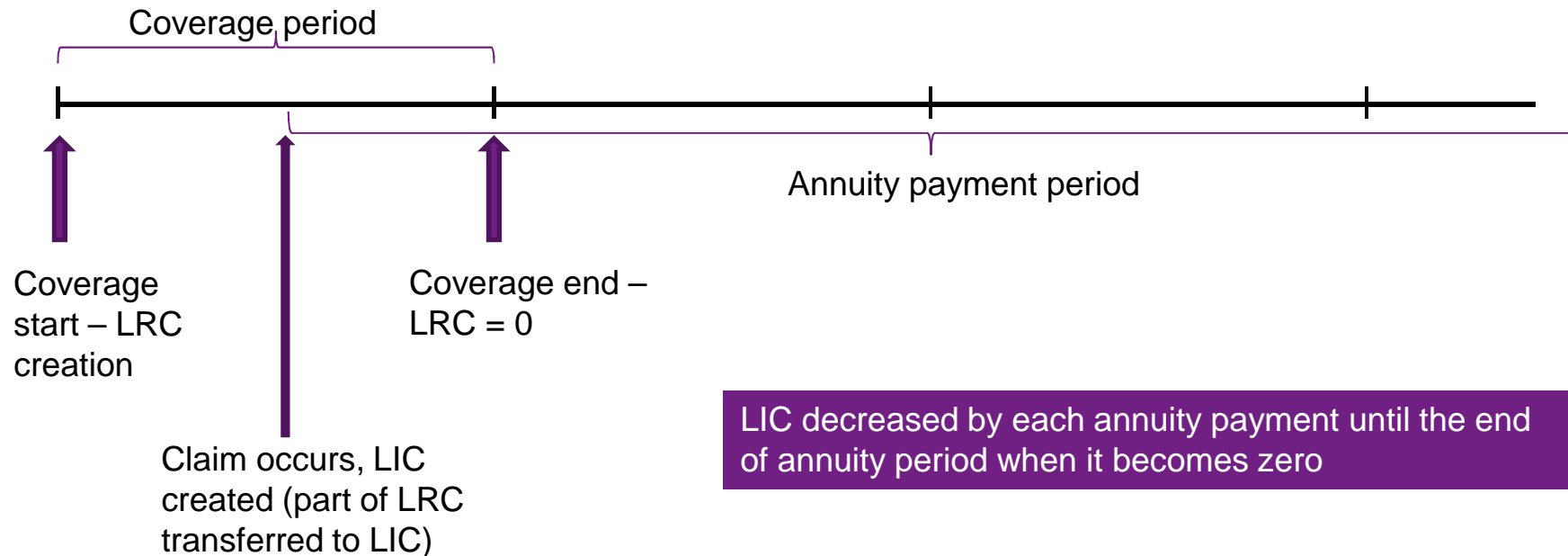
Latest TRG (April 2019) proposal to improve the definition as it is in Basis for Conclusion:

*“...an investment component should be defined as the amount that the contract requires the entity to repay to a policyholder in all circumstances, regardless of whether the insured event occur...”*



# Liability for remaining coverage (LRC) vs Liability for Incurred claims (LIC)

## MTPL contract for 1 year, annuity claim



## Annuity contract from the example

- When is LIC created (if ever)? When is LRC released? Where are contract boundaries?
- What is my claim? Is it only one claim?

## Coverage units

How to set coverage units?

Definition of coverage units

- Statutory profit
- Volume based
  - asset under management
  - technical reserve
- Coverage units = investment part coverage units (e.g. interest on reserve)  
+ risk part coverage units (e.g. annual annuity)

Deferred annuities during deferral period (B24)

- Insurance contract (?)
- Investment contract (?)

## Other issues

Amortization period for acquisition expenses

- Deferral period or whole life of the contract?
- B125 supports deferral period

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74.00	0.026214	0.84723		847.23	78.30		13.05

## IFRS 17 P&L – time 0

IFRS 4		IFRS 17	
Premiums	17 799.17	Insurance revenue	
Investment income		• Expected claims and expense	
Incurred claims and expenses	625	Insurance service expense	
Change in insurance contract liabilities	16 617.29	• Incurred claims and expenses	
Profit or loss	556.87	Insurance service result	
		Investment income	
		Insurance finance expense	
		Net financial result	
		Profit or loss	0
		Discount rate changes on insurance liability ( <i>optional</i> )	
		Total comprehensive income	0

Day 1 Profit for IFSR 17 is zero, however unrealized profit, CSM, equals:  
 $CSM = 313.58 = PV\_income - PV\_outgo + RA$

## IFRS 17 P&L – time 1

IFRS 4		IFRS 17	
Premiums		Insurance revenue	1 117.21
Investment income	389.52	• Expected claims and expense	1 095
Incurred claims and expenses	1 095.22	Insurance service expense	1 095
Change in insurance contract liabilities	-874.48	• Incurred claims and expenses	1 095
Profit or loss	168.78	Insurance service result	22.21
		Investment income	389.52
		Insurance finance expense	197
		Net financial result	192.51
		Profit or loss	214.72
		Discount rate changes on insurance liability ( <i>optional</i> )	
		Total comprehensive income	214.72

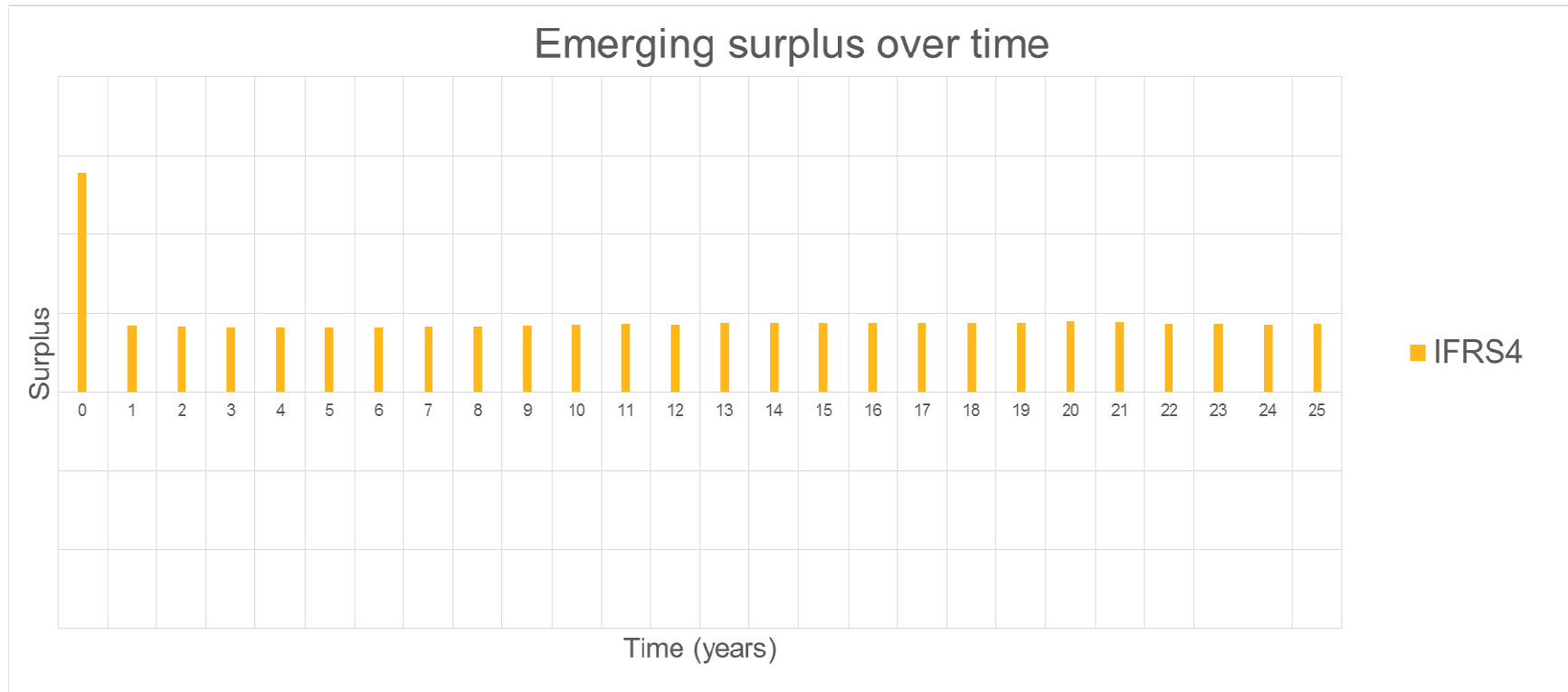
## IFRS 17 P&L – time 1

Expected claims	990
Expected expense	105
Release of CSM to P&L	17.07
Release of risk adjustment to P&L	5.14
Insurance revenue	1 117.21
Incurred claims	990
Incurred expense	105
Insurance service expense	1 095
<b>Insurance service result</b>	<b>22.21</b>
Investment income	389.52
Insurance finance expense	197
<b>Net financial result</b>	<b>192.51</b>
<b>Profit or loss</b>	<b>214.72</b>
Discount rate changes on insurance liability ( <i>optional</i> )	
<b>Total comprehensive income</b>	<b>214.72</b>



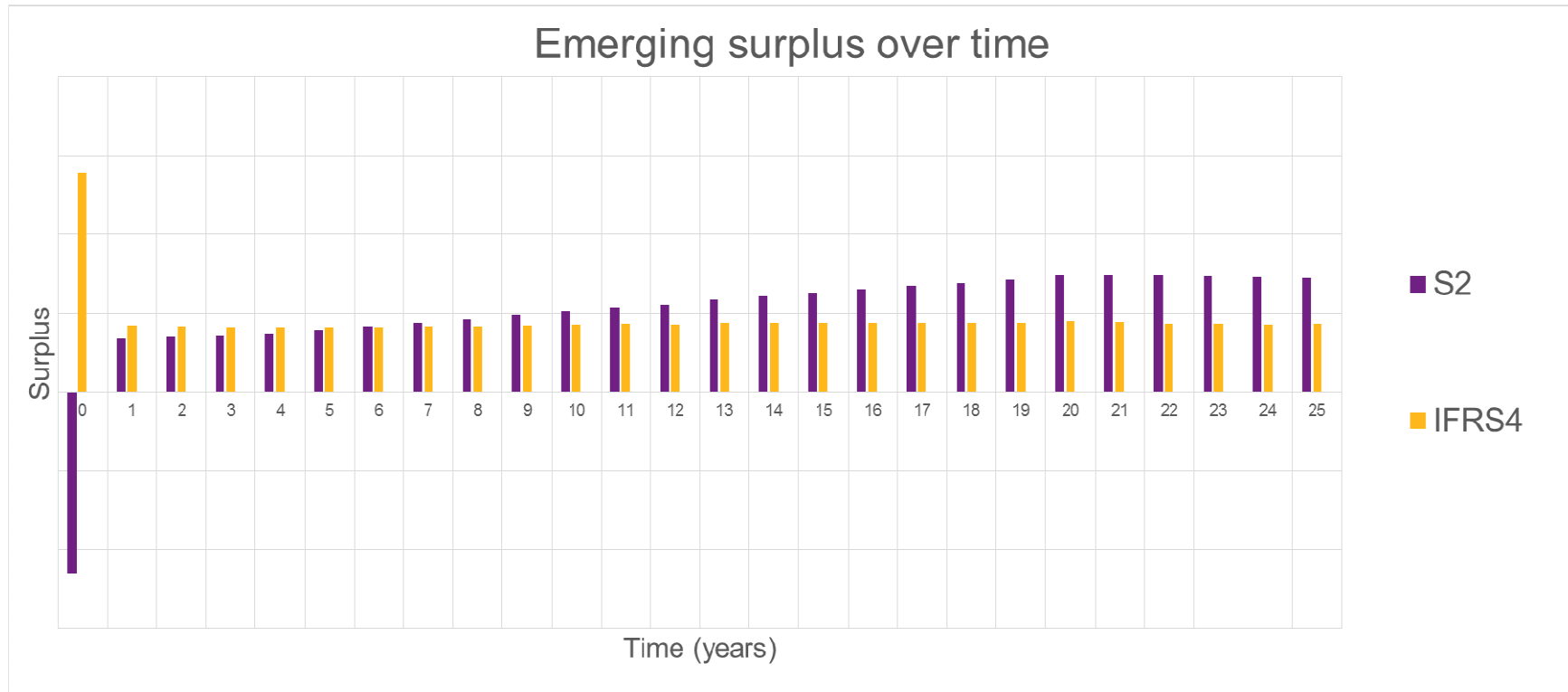
# Example: Annuity projections

## Emerging surplus under IFRS 4, IFRS 17, Solvency II (net of SCR)



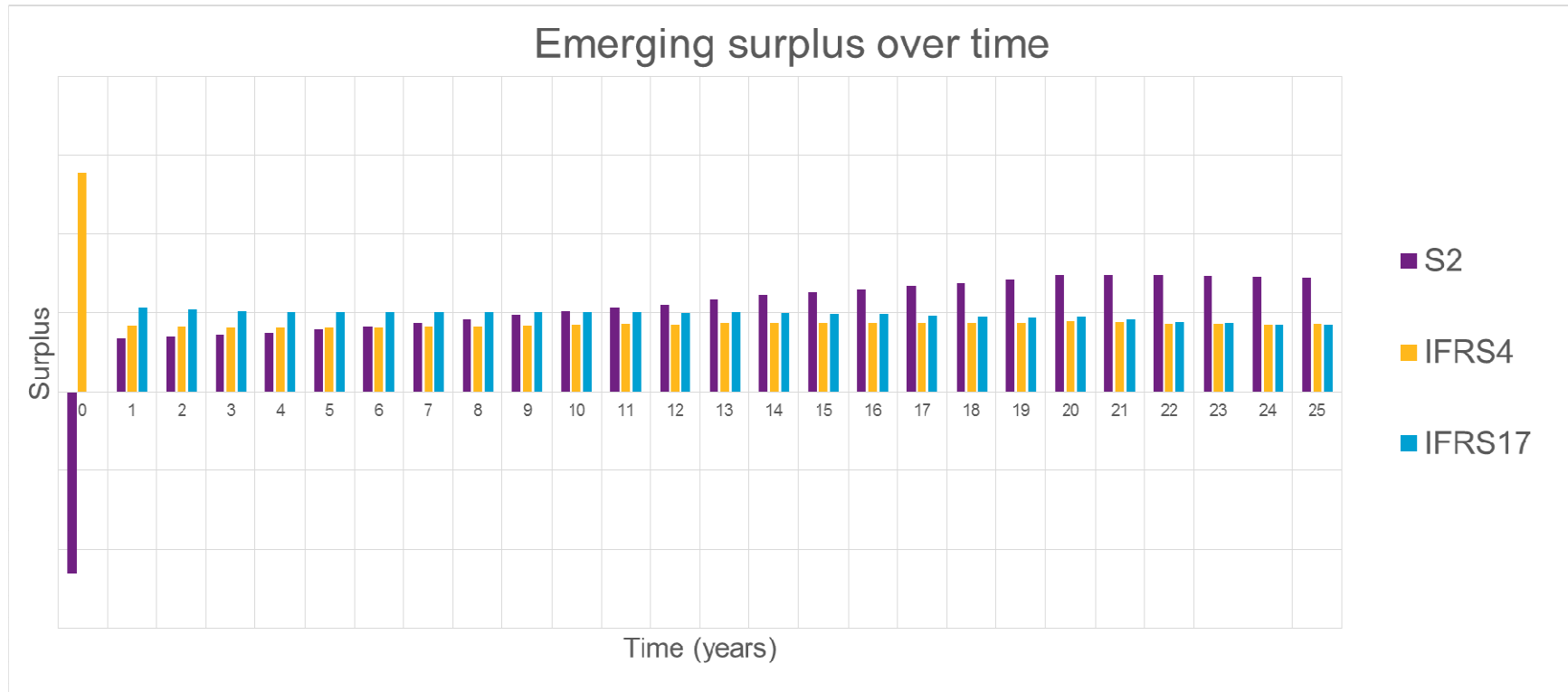
# Example: Annuity projections

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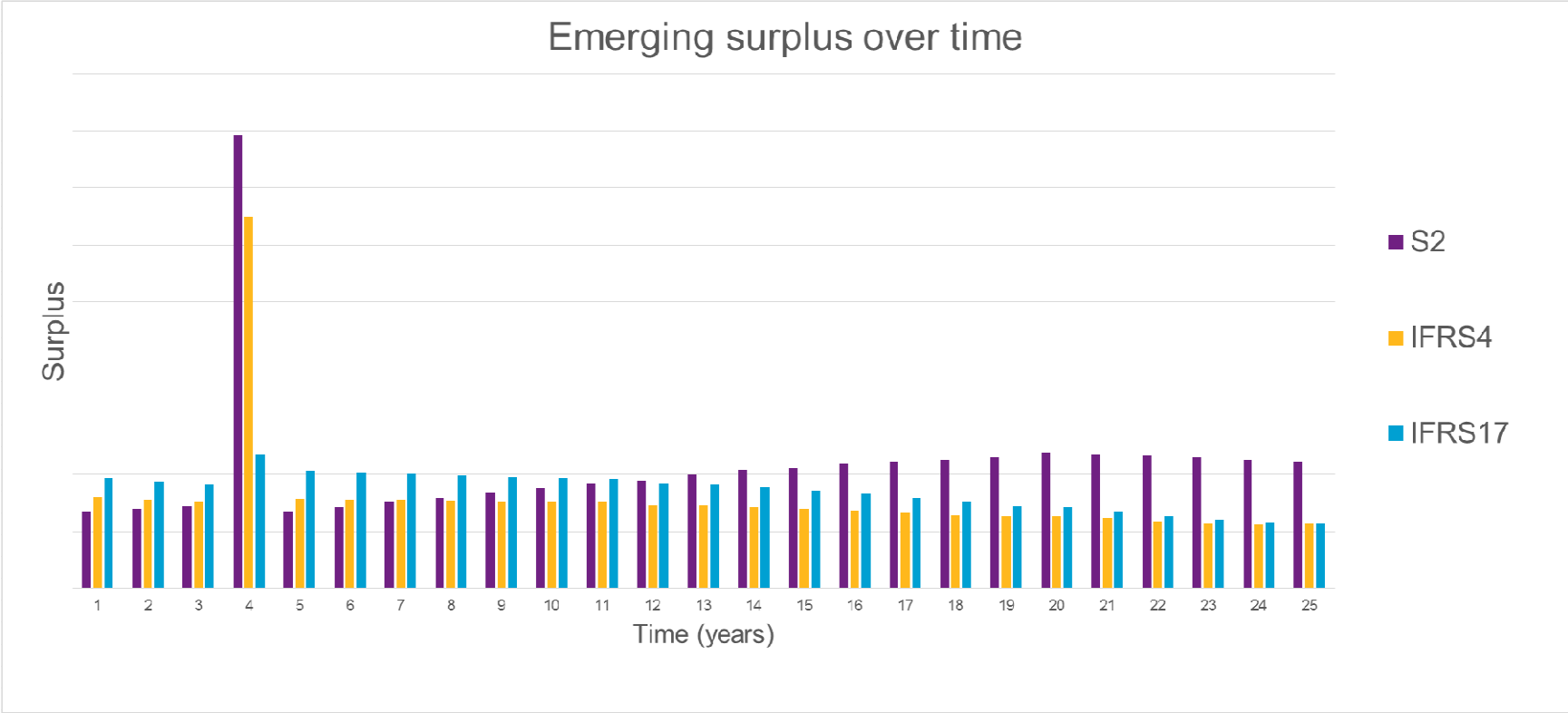
# Example: Annuity projections

## Emerging surplus under IFRS 4, IFRS 17, Solvency II (net of SCR)

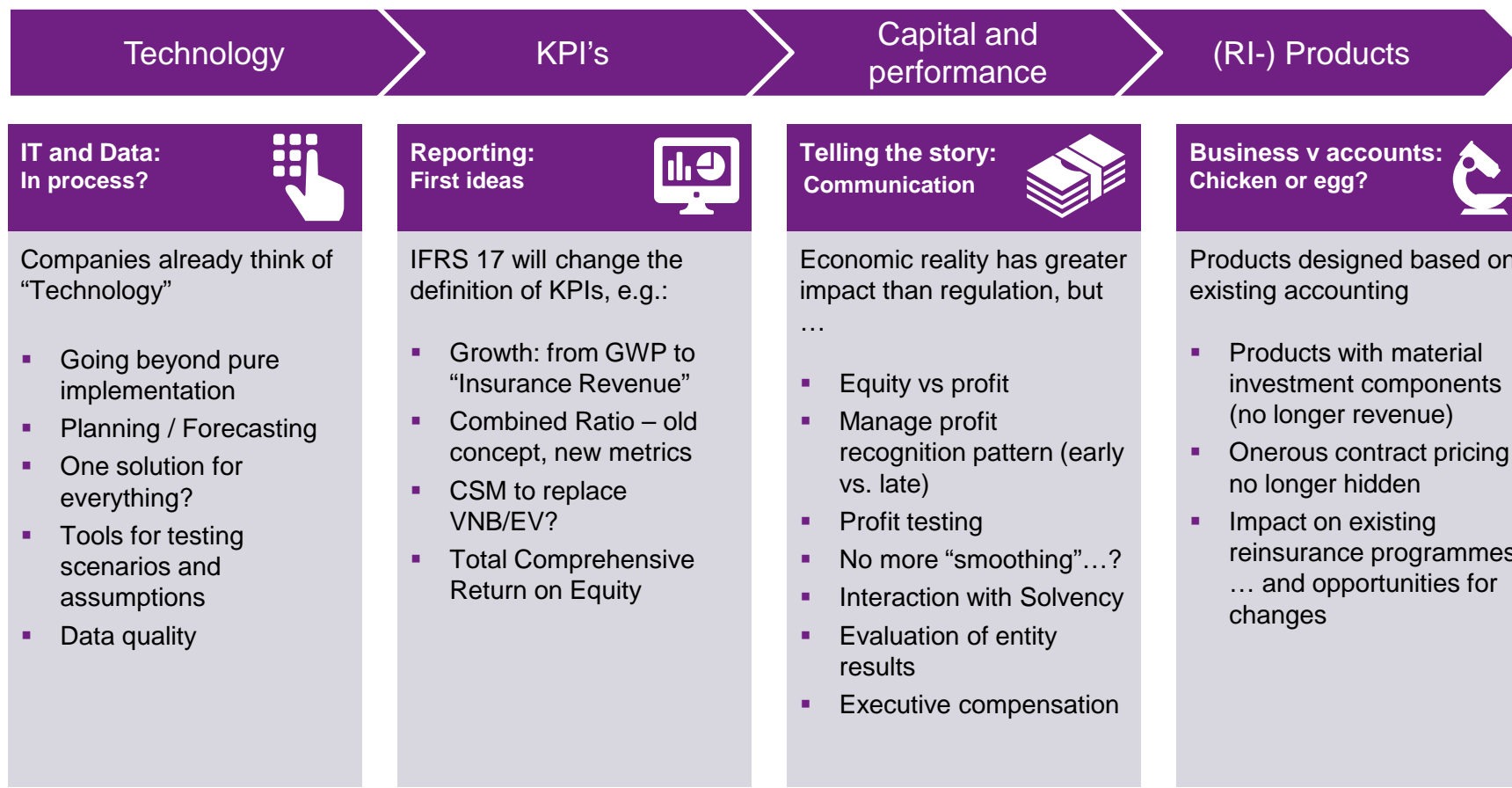


# Example: Annuity projections

## Positive mortality experience variance (+10%) in year 4



# Future business implications



# Thank you

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