The deferral of IFRS 17, and the impact of COVID-19

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Contents

Introduction

At its meeting on 17 March 2020, the International Accounting Standards Board (IASB) agreed to defer the effective date of IFRS 17 Insurance Contracts (IFRS 17), including the amendments, to annual reporting periods beginning on or after 1 January 2023.

The IASB also agreed to extend the fixed expiry date of the temporary exemption from applying IFRS 9 Financial Instruments (IFRS 9) for qualifying insurers (as contained in IFRS 4), so that all entities must apply IFRS 9 for annual reporting periods beginning on or after 1 January 2023. Early adoption of IFRS 17 is permitted, provided an entity also applies IFRS 9.

Options to consider

The deferral of the effective date of IFRS 17 and 9 leads to several options for insurers and reinsurers for their accounting change implementation roadmap.

The table below describes a few options that insurers can take:

Options to consider	Advantages	Disadvantages
Continue on the current project timetable to adopt IFRS 17 and IFRS 9 in 2022. Continue project at the current pace.	‣ Contains the cost of implementation ‣ Frees up key resources sooner than other options ‣ Removes the requirement to reassess the overall IFRS 17 program timeline	‣ Early adoption could result in an insurer or reinsurer being the outlier in the market ‣ Leaves less time for testing and learning from others ‣ Does not take into account potential COVID-19 impact
Continue on the current implementation project timetable, but only adopt IFRS 17 and IFRS 9 in 2023 for public financial statements	‣ Leaves more buffer time that can be used for testing or for any unplanned contingencies, such as the impact of COVID-19 on the project timelines ‣ Allows for more effective and robust implementation and parallel runs	‣ More resource intensive in the short term and hence more costly ‣ Increased risk that further changes may be required during the final year before public adoption, particularly for IFRS 9 information as IFRS 9 transition rules do not allow IFRS 9 to be applied to financial instruments that are no longer recognized on the balance sheet at the beginning of 2023
Slow down the IFRS 17 implementation project timetable and adopt IFRS 17 and IFRS 9 on 1 January 2023	‣ Enables the project to continue and momentum is preserved, but possibly at a slower pace ‣ Parts of the project are deferred or the timelines extended ‣ More room for contingency, testing and remediation in the plan ‣ Some IFRS 17 resources can be diverted to other projects in the short term or more internal resources can replace external resources	‣ Could lead to substantive increase of costs over the project lifespan (especially toward the end of the project) ‣ Increases the risk of failure due to delayed testing, transition and parallel run
Pause the project, and adopt IFRS 17 and IFRS 9 in 2023	‣ Saves costs now as project is put on hold in the short term ‣ Enables IFRS 17 resources to be diverted to other projects in the short term ‣ Allows additional time for vendors to develop their IFRS 17 solutions	‣ Loss of momentum ‣ Need to free up and retrain resources when the project is restarted later ‣ System vendors and experienced consultants may not be easily available when the project is restarted ‣ Higher risk to meeting project deadlines on time ‣ Experience from Solvency II shows that postponed projects can be much more expensive in the end due to heavy last-minute reliance on external resources ‣ Leaves less time for knowledge transfer and retention

For those insurers that have not yet started their implementation programs, the delay to the effective date of IFRS 17 provides an additional year to meet the deadline in 2023. However, projects should be started without delay, due to the complexity of the change required.

COVID-19 impact on IFRS 17 and IFRS 9 implementation

The impact of the coronavirus outbreak is still evolving. Many countries have imposed measures such as travel restrictions, quarantines and social distancing that have resulted in a significant drop in demand for goods and services and major supply chain disruptions. There is also high volatility and liquidity shortage in the financial markets. Insurers and reinsurers should allow for the disruption caused by this pandemic when revisiting their implementation plans. What will the impact of COVID-19 be on project resourcing and timelines:

- Resources may have to be reallocated from IFRS 17 to other projects in order to prioritize responses on the developing global pandemic crisis as the demand for already scarce resources such as accountants and actuaries increases.
- IT systems and network may need to be upgraded to support remote working.
- IT resources and system CPU, storage and network capacity that were originally reserved for the use by the IFRS 17 and 9 project may need to be diverted to other more urgent initiatives to mitigate the COVID-19 consequences.
- Face-to-face meeting restrictions may impact easy access to vendors and suppliers and reduce the efficiency of the day-to-day project operations.
- Company financial and solvency positions may deteriorate, putting pressure on costs and IFRS 17 implementation budgets.
- Some regulators are pausing consultations on the development of new financial or regulatory frameworks, taking pressure away from current and ongoing industry changes.

We suggest insurers and reinsurers consider adopting an agile implementation methodology for the IFRS 17 and 9 program and review the overall implementation plan frequently as the pandemic situation evolves.

The COVID-19 outbreak has significantly increased the need for and importance of agile project techniques to ensure the project can continue to progress as planned on a "no regrets basis". This can be achieved by using separate (and often remote working) "sprint teams", to ensure overall program delivery as planned while at the same time addressing issues in smaller test teams to minimize disruption. This ensures that, when there is less physical interaction between the multiple sprint teams, workstream interdependencies don't become a bottleneck for the entire program.

Recommendations

Preparers should address the following recommendations as a result of the deferral of the effective date for IFRS 17 and IFRS 9, and the COVID-19 pandemic:

Reassess overall program and workstream time frames, as well as key milestones allowing for the new effective date

Preparers can use the opportunity of the deferral of the effective date for IFRS 17 to take stock of the current position of their IFRS 17 and 9 program and time frames. This would include assessing:

- The progress to date on the accounting policy papers, actuarial model changes, proforma financial statements design, overall solution design (covering data requirements, system specifications and process changes), chart of account changes, transition planning, user training and documentation, parallel run preparations and handover planning to business as usual (BAU).
- The progress made on the planned system solution, including vendor selection, data preparation, system customization and configuration, testing tools and procedures, dry run and go-live plan.
- The planned changes to the external financial reporting templates and management reporting tools, including new KPI framework and CFO dashboards.
- The definition of a detailed target operating model with clear roles and responsibilities for the combined finance and risk operations under the new IFRS 17 and 9 reporting regime.
- The development of a clear and compelling investor story for listed insurers who will need to prepare the market for the significantly changed financial statements presentation, combined with enhanced transparency and comparability of the true business performance through much more granular and standardised disclosures.
- The linkages and key interdependencies of the IFRS 17 and 9 program with other in-flight programs.
- The effectiveness of the current project governance structure including the right balance between internal and external resources.
- The adequacy of the originally allocated project budget under the new circumstances (can be verified through benchmarking with peers).
- The availability of key resources and the status of development of IFRS 17 vendor solutions.

Key milestones can be adjusted if the preparer is not adopting IFRS 17 and IFRS 9 early. This gives more time to plan and implement a well-controlled and robust IFRS 17 (vendor or self-built) solution. It also provides the preparer additional time for better analysis and understanding of the results after implementing the vendor solution.

Update accounting policies and revisit policy choices in response to the revised standard

Even though the IASB decided not to make an amendment for some fundamental topics (e.g., the annual cohort requirement), there are still a number of amendments tentatively agreed to during the recent redeliberation process that may have a significant impact on implementation efforts.

Decisions regarding the recovery of losses by reinsurance held, investment expenses included in fulfillment cash flows, recognition and impairment of assets arising from insurance acquisition cash flows, and (interim) reporting frequency will require significant evaluation. It may also require preparers to rethink some of their earlier IFRS 17 decisions. Accounting policies and policy choices may need to be revisited and revised considering the changes to IFRS 17.

Reassess the current status of system design and configuration requirements in response to the revised standard and any changes to accounting policies

The revisions to the standard and any resulting changes to accounting policies could trigger a system redesign or reconfiguration and/or require different data inputs. Preparers should engage with their system architects and vendors to understand the impacts of these changes and adjust the system design specifications where needed. Additionally, many off-the-shelf vendor solutions are still being developed and will require more time to embed the latest amendments and be ready for mass market deployment.

As a result, processes and systems designs may need to be adapted in response to the amended IFRS 17 standard, thus requiring further development work and additional time added to the IFRS 17 implementation plan.

Align testing and parallel-run strategy and planning, as well as building sufficient controls over the end-to-end IFRS financial reporting process

Keeping the development on schedule and allowing more time for testing and remediation after tests and dry runs will be valuable during implementation. Lessons learned from Solvency II projects highlight that testing and remediation through dry runs are often neglected, resulting in improvements to processes being made post-implementation.

Most large insurance and reinsurance companies that are developing central IFRS 17 and 9 solutions have local country implementation as one of the last steps in their programs. This will result in local teams not having enough time to understand the new system and make it part of their BAU finance and risk operations. Therefore, these companies should conduct a country readiness assessment to confirm that they understand the amount of time and effort required to roll out the centrally developed solution to the local countries in a safe and controlled manner.

User trainings would also need to be conducted on the detailed workings of the multiple system components (data input; cost allocations; contractual service margin (CSM) calculations; chart of accounts (COA) design; posting framework; accounting entries; mapping to general ledger (GL); extract, transform and load (ETL) interfaces, reporting tools and workflow manager). The updates to accounting policies and resulting system design changes will require a lot of time for verification, testing, dry runs and training.

Update and engage key stakeholders (including auditors, regulators and analysts) on next steps and expected impacts

The business impacts of IFRS 17 need to be understood and communicated to a wide range of internal and external stakeholders. Given the scale of this change, investors and other key stakeholders will want to understand the likely impacts as early as possible. Preparers can spend more time on understanding the financial outcomes, and on communications with investors and regulators. They can also act early to mitigate any undesired impact to the business by trying to optimize the reported outcomes and assess the sequence of any wider change program.

Additionally, many countries will follow different (later) adoption dates and might adopt slight variations of the IASB standard for local statutory reporting requirements. The alignment of IFRS 17 Group reporting with local regulatory and tax reporting will require time and effort.

Summary

The decision of the IASB means that preparers are effectively granted an additional year (until 2023) to prepare for the initial application of IFRS 17 and IFRS 9, compared to the proposals in the June 2019 Exposure Draft. Based on anecdotal evidence from the market, the insurers and reinsurers who are already well progressed with their IFRS 17 implementation will likely use the extra year for further system development, testing, data preparation, parallel run and user training. COVID-19 is likely to further impact the pace of the IFRS 17 implementation, and companies may need to revise their plans in light of this new uncertainty. The final IFRS 17 standard is expected to be issued by the IASB in June 2020.

In our view, continuing the implementation project at current pace but adopting IFRS 17 and IFRS 9 on 1 January 2023, seems to hold the most merit for most insurers and reinsurers. This option gives them time to reassess their implementation program, revisit policy choices in view of the amendments to the standard, do more systems testing and have buffer time for contingencies while dealing with the evolving COVID-19 situation at the same time.

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