McGowan Program Administrators

# An Introduction to IFRS 17 for CPAs

A major change is about to sweep through the accounting departments of the world's insurance companies in the next three years. A new global standard called IFRS 17 Insurance Contracts goes into effect in 2021, obliging publicly traded insurance companies around the world to adopt similar financial reporting models to provide more transparency and consistency to investors, regulators, and others who monitor the industry.

Issued by the International Accounting Standards Board (IASB), IFRS 17 applies to 450 global insurers with assets worth $13 trillion, according to the IFRS Standards Fact Sheet. Those who need to be familiar with the standards include:

- CPAs working for global insurance firms.
- CPAs working in a company acquired by a global insurance firm.
- CPAs moving into the global insurance industry.
- Financial analysts covering the insurance industry.
- Investors looking to buy insurance stocks or acquire insurance companies.
- Regulators who monitor the insurance industry.

This report will give CPAs a concise introduction to IFRS 17 and links to more in-depth resources for further study. It also will provide a useful summary for company stakeholders outside the accounting department who need to understand the importance of the new global standard for insurance contracts.

## The background of IFRS 17

IFRS 17 replaces IFRS 4, which was introduced in 2004. While IFRS 4 was a good start, there were many inconsistencies that made it difficult to compare insurance companies operating in different countries, or to compare insurers to companies in other industries.

"IFRS 17 provides consistent principles for all aspects of accounting for insurance contracts," the IFRS Standards Fact Sheet says. "It removes existing inconsistencies and enables investors, analysts, and others to meaningfully compare companies, contracts, and industries."

It's important to understand that IFRS 17 stands apart from U.S. GAAP (generally accepted accounting principles). Though U.S. GAAP is considered the gold standard, many nations and companies worldwide do not abide by it. IFRS 17 was designed specifically for the needs of global insurers affected by a wide variety of regional economic conditions, national laws, and local regulatory concerns.

Something else to bear in mind: IFRS 17 gives accountants and companies a degree of latitude in interpretation that contrasts sharply with other standards and regulations.

"IFRS 17 is truly principles-based, which in most cases will mean it is the insurer's responsibility to ensure policies and disclosures comply with the standard's requirements, rather than it being able to rely on prescriptive and detailed rules," the consultancy Willis Towers Watson said in a news release.

*"IFRS 17 provides consistent principles for all aspects of accounting for insurance contracts. It removes existing inconsistencies and enables investors, analysts, and others to meaningfully compare companies, contracts, and industries."*

## Key Changes in IFRS 17

The full scope of the changes in the new standard is vast. Indeed, a report from KPMG titled "Insurance Contracts, First Impressions" expends 186 pages explaining the contours of the standards to insurance accounting professionals.

In sum, the principles of IFRS 17 improve reporting on the value of insurance obligations and on potential profitability, according to IFRS Standards Fact Sheet:

- Insurers will switch to measuring insurance contracts at their current value; the old standard allowed companies to measure contracts with outdated data.
- Time value of money (TVM) will be used to estimate the payouts required to settle claims; the old standard did not require TVM.
- Insurance contracts will be measured based on the obligations the contacts create. Under the old standard, companies could use their investment portfolios to measure insurance contracts.
- Insurers will publish consistent data on the components of the profits their contracts generate currently and in the future. The old standard allowed much more inconsistency.

The IASB gathered a broad range of feedback to develop the standards, including more than 600 comment letters; discussion forums in 18 countries; and 900-plus meetings with investors, analysts, actuaries, regulators, and many more.

Next up, we'll summarize how these new principles affect the industry and CPAs.

## Major impacts of IFRS 17

KPMG's "First Impressions" report illustrates the depth and breadth of the switch to IFRS 17. Among the highlights:

- **Higher volatility.** The new standard's reliance on TVM (time value of money) requires companies to base their calculations on current market discount rates, which is likely to introduce volatility in financial results and equity. The upside of the volatility is that it'll be easier for investors and analysts to detect mismatches between assets and liabilities.
- **Clarity on performance.** The impact of financial risks on a company's results are to be shown separately from insurance performance. This gives a clearer picture of what's driving an insurer's profits.

- **Resource scarcity.** Companies might have trouble finding enough people with the right training to translate the standard's theories into practice.

The transition to IFRS 17 will require a major commitment of people, time, and expertise in the years to come, says Kamran Foroughi, a director at Willis Towers Watson: "The new standard will impact profit, equity, and volatility, as well as reserving and financial reporting processes, actuarial models, IT systems, and potentially executive remuneration, so insurance companies should not underestimate the work required. The additional complexity will also affect communication with investors."

CPAs in the global insurance industry interested in helping their clients and their colleagues implement the standard should check out the Transition Resource Group for Insurance Contracts, which is recruiting members to organize meetings, webinars, and other activities.

## Making the best of the transition to IFRS 17

The complexities of getting the world's insurers to switch to a comprehensive accounting standard cannot be underestimated. But gaining a clearer picture of insurance companies' financial status will be well worth the trouble. After all, in the 2008 financial crisis, the bailout of a large insurer helped stave off a global calamity.

Insurance is a big business that requires robust accounting standards. Helping insurers implement those standards presents a wealth of opportunity to CPAs who can devote the time and energy to master the subtleties of the new rules and reach out to insurers who need guidance implementing the standards.

## Resources for further study

"IFRS Standards Fact Sheet," IASB

"Insurance Contracts, First Impressions," KPMG

"IFRS 17, What does it mean to you?" Deloitte

"IFRS FAQs," AICPA

"Insurance Contracts," IFRS

Transition Resource Group for Insurance Contracts

## For more information, contact:

**Dogan Tuncel**
Phone: 440.333.6300
dtuncel@mcgowanprograms.com