IFRS17 – Lessons learned

March 2024

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02 Solvency II to IFRS 17 Comparison and Reconciliation

03 IFRS 17 Current Challenges

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1. Impacts of IFRS17 adoption

Strong underlying business fundamentals not impacted by IFRS 17

01

Business Strategies Unaffected:

No impact on Business Strategies

02

Medium term financial objectives:

Increase in underlying ROE; maintain underlying EPS growth and underlying dividend payout ratio

03

Shareholder Equity Transition:

At transition, 15%-20% of shareholders equity transfers to liabilities, largely to establish the Contractual Service Margin (CSM)

04

Transitioning to Growth:

Mid-Single digit reduction to underlying net income in 2022 comparative year; expective positive underlying net income growth from 2022 (IFRS 4) to 2023 (IFRS 17)

05

Stability Enhanced:

IFRS 17 underlying net income will be more stable

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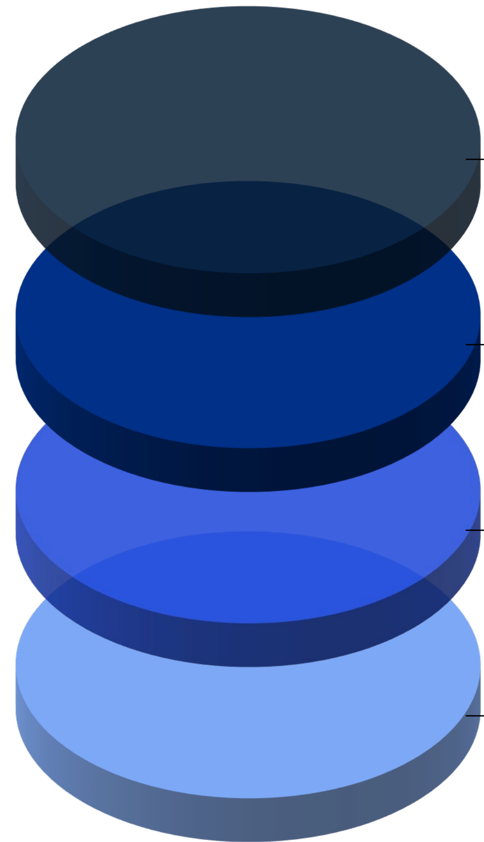
Overview of key IFRS 17 changes



01
New business gains

Pricing gains are deferred and recognized over time through CSM amortization, whereas losses (new business strain) are recognized in net income at origination

02
Discount rates

Removal of direct link between the asset and liability discount rates and the new valuation of certain minimum guarantees expected to increase reported net income volatility

03
Timing of investment profits

Value of investing activity gains / changes to investment strategies will be recognized as earned

04
ACMA

Insurance risk changes will be reflected in CSM and amortized over life of insurance contracts

Financial risk changes (e.g., changes to discount rates) continue to be recorded through income for most products (exception in Variable Fee Approach products, such as segregated funds, which are recorded in CSM)

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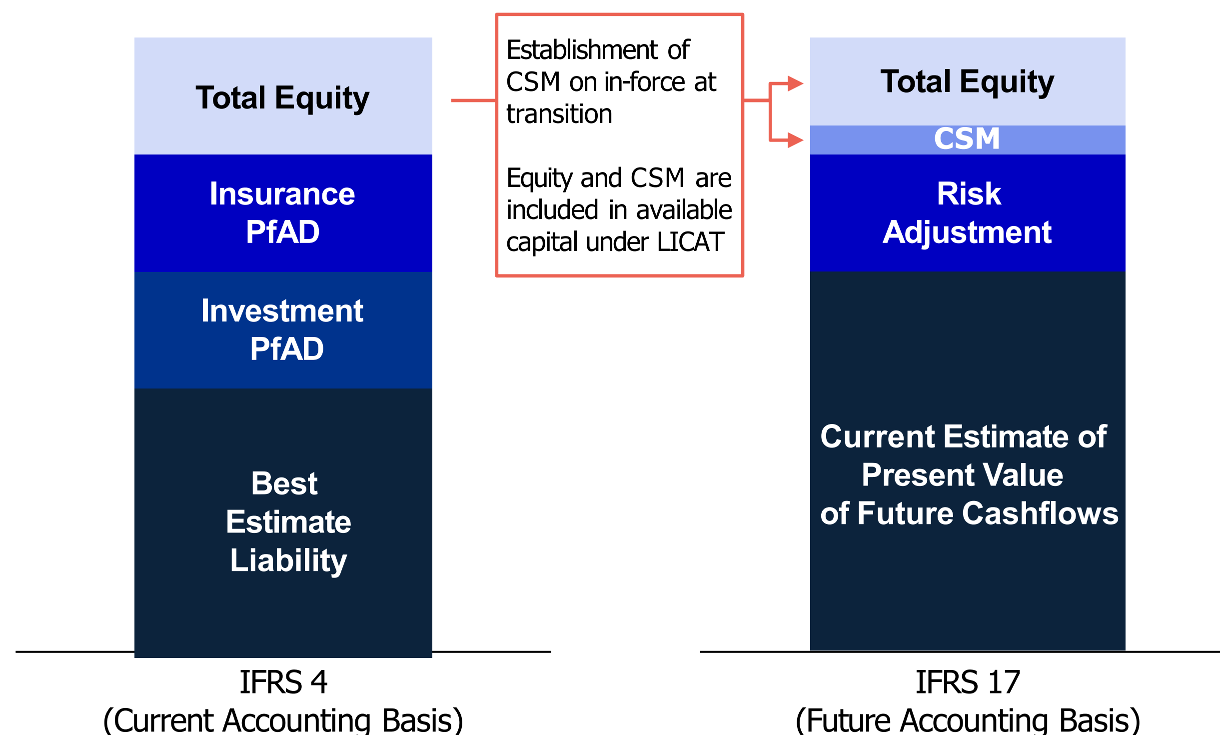
At transition, insurance liabilities will increase primarily due to establishing the CSM

- Under IFRS 4, new business gains are recognized immediately in income. Under IFRS 17, **new business gains** are recorded as CSM and **recognized over the life of the contract.**
- Upon implementation, companies presented our financial position as though IFRS 17 had always applied and set up a CSM on their in-force insurance business
- Establishing the CSM is the main driver of the increase in the insurance contract liabilities at transition
- Overall, we saw, on average, an **increase in insurance contract liabilities** with a corresponding **reduction in equity of approximately 20%**
- In average **medium-term core ROE target** will be **increased upon transition** due to IFRS 17 from 13%+ to 15%+

Illustrative example of balance sheet impact[2]



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Confirming medium-term financial and operating targets

		IFRS 4	IFRS 17
Financial Targets[1] (medium-term)	Core EPS growth	10-12%	
	Core ROE **(REVISED)**	13%+	**15%+**
	Leverage ratio (adjusted for CSM)	25%	
	Dividend payout ratio **(REVISED)**	30-40%	**35-45%**
	CSM balance growth **(NEW)**	n/a	**8-10%**
	New business CSM growth **(NEW)**	n/a	**15%**
Financial Targets[1] (2022+)	Expense efficiency ratio	<50%	
Supplemental Goals[1] (2025)	Core earnings from highest potential businesses	75%	
	Core earnings from Asia region (Insurance + WAM)	50%	
	Core earnings from LTC and VA	<15%	

- Core ROE target will increase to 15%+ driven by the expected changes to core earnings and equity
- No expected changes to dividend per share and growth trajectory, as a result dividend payout ratio target range will be increased to 35%-45%
- New CSM KPIs highlight the importance of CSM growth and are indicative of future earnings generation capability

See appendix for KPI definitions. As emerging industry practice evolves, KPI and KPI definitions may be updated.

Note: See "Caution regarding forward-looking statements" above. [1] For more information on our medium-term financial and operating targets, see the Management's Discussion and Analysis in our most recent interim and annual reports.

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KPI definitions[1]

Term		Definition
Profitability	Core EPS growth	Year over Year core EPS growth
	Core ROE	$\frac{\text{Core earnings} - \text{Preferred dividends} - \text{Other equity distributions}}{\text{Average common shareholders' equity}}$
	Expense efficiency ratio	$\frac{\text{Core general expenses}}{\text{Core general expenses} + \text{Pre-tax core earnings}}$
Financial Strength	Leverage ratio	$\frac{\text{LT debt} + \text{Capital instruments} + \text{Preferred shares}}{\text{LT debt} + \text{Capital instruments} + \text{Total equity} + \textbf{CSM balance}}$
Growth	New business CSM growth	**Year over Year new business CSM**
	CSM balance growth	**Year over Year CSM balance growth**
	Core earnings from highest potential businesses	$\frac{\text{Core earnings from highest potential businesses}}{\text{Total core earnings}}$
	Core earnings from Asia region (Insurance + WAM)	$\frac{\text{Core earnings from Asia region}}{\text{Total core earnings}}$
Other	Core earnings from LTC and VA	$\frac{\text{Core earnings from LTC} + \text{VA}}{\text{Total core earnings}}$
	Dividend payout ratio	$\frac{\text{Dividends per common share}}{\text{Core EPS}}$

[1] As emerging industry practice evolves, KPI and KPI definitions may be updated.

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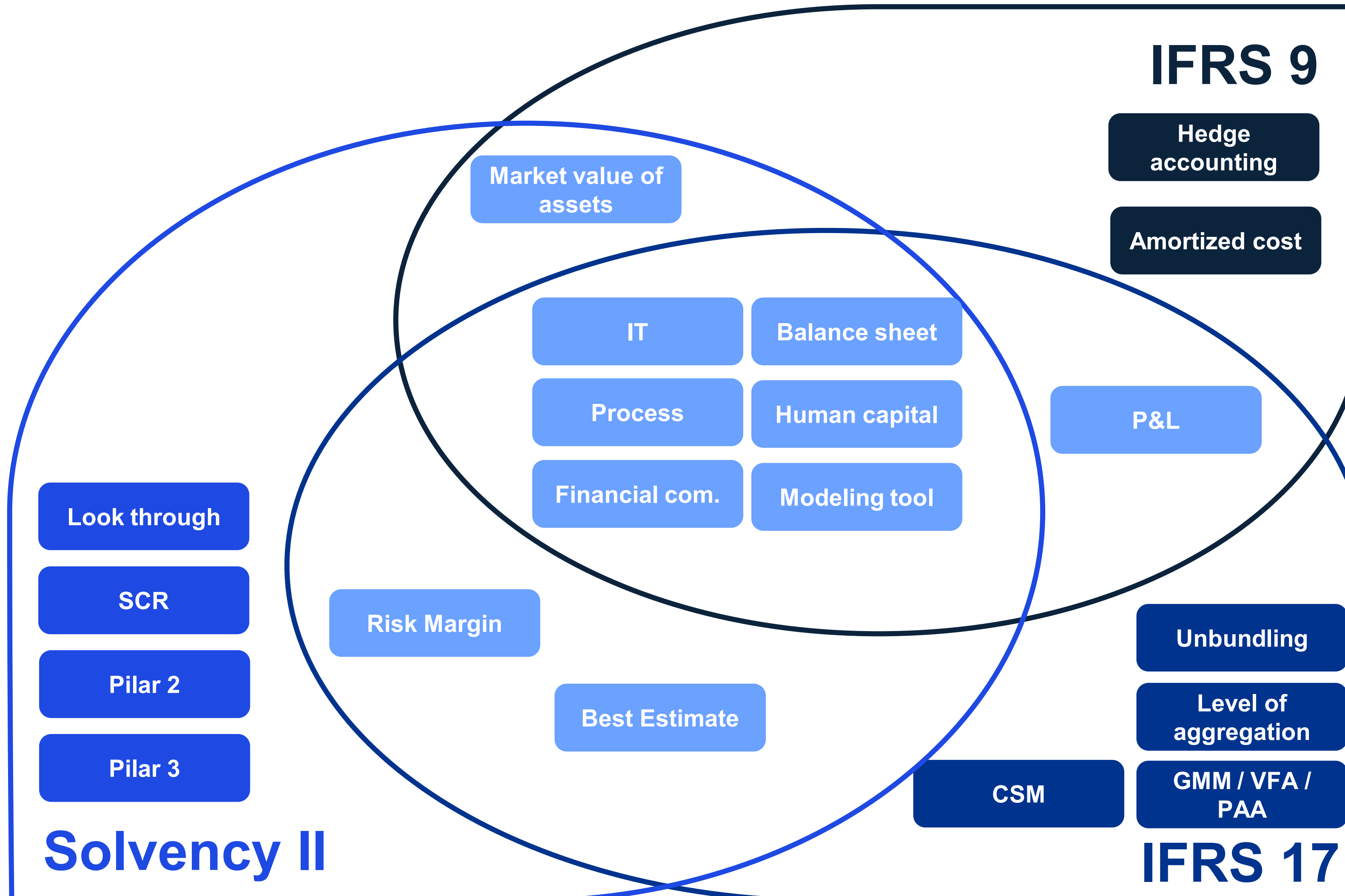
2. Solvency II to IFRS 17Comparison and Reconciliation

Introduction



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Key Differences

Solvency II		IFRS 17
No CSM recognition (released in own funds)	**CSM**	CSM absorbs shocks and amortizes each period
Entity* LoB	**Granularity**	Portfolio *1 Yr cohort* Group
Cost of Capital method(6% and 100% SII ratio)	**Risk Adjustment**	Method to be defined by the entity
Swap curve+ volatility adjustment+ UFR	**Discount Rate**	Top down or bottom up approach
Cash flows according to SII principles	**Best Estimate**	Cash flows according to IFRS 17 principles
X	**P&L**	P&L IFRS 17
QRT and narratives	**Reporting**	Financial statements (incl. annexes)
Quarterly	**Reporting Period**	Monthly, quarterly, semestrial, annual(depending on the entity)

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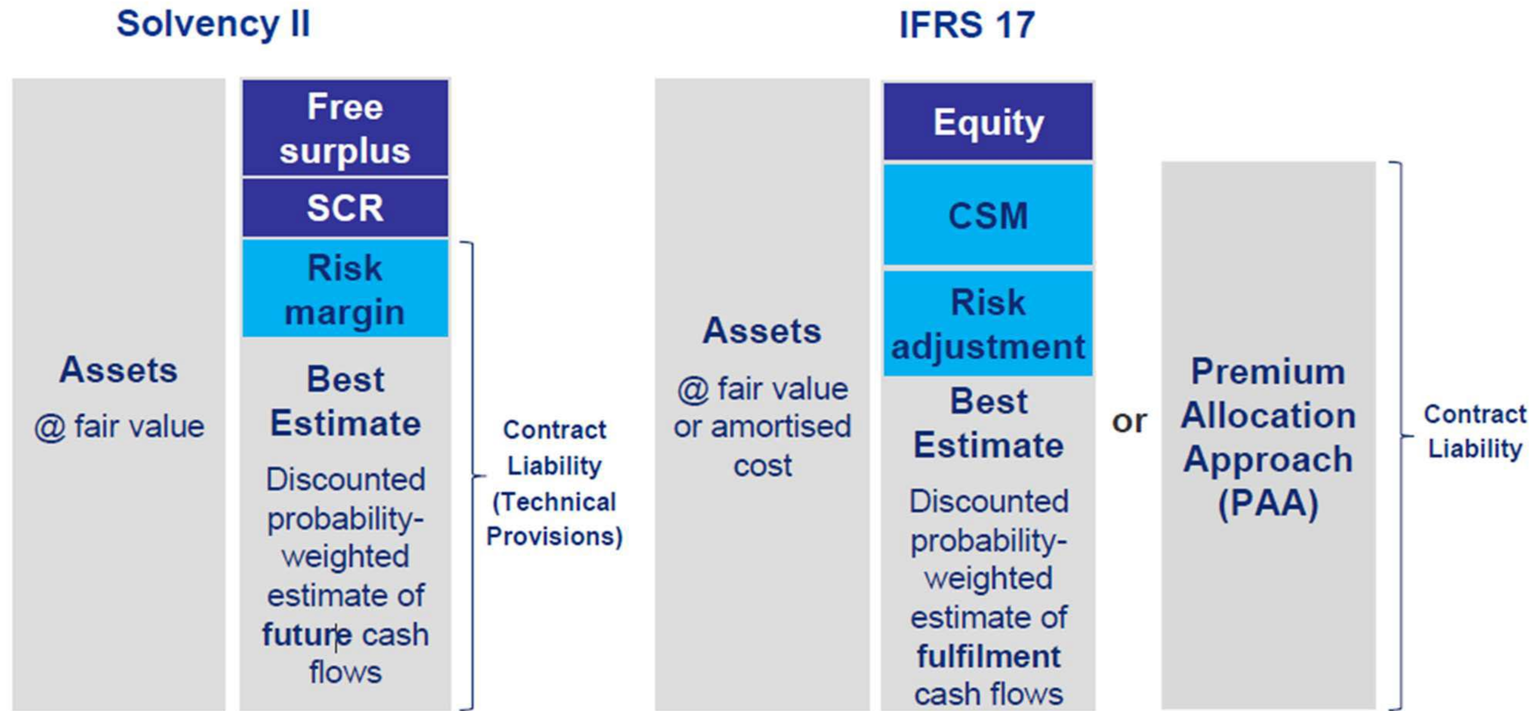
Overview of the Balance Sheet



Relative size of liabilities, capital requirements and margins are for illustration purposes only and could differ significantly by company or product line.

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Main Similarities / Differences- 1/2

- 🔴 Significant impact
- 🟠 Medium impact
- 🟢 Slight/no impact

Item	Similarities / Differences / Nature of challenge	Impact
Definition and scope	IFRS 17 is more restrictive than Solvency II	Medium (orange)
Unbundling	Under IFRS 17, entities may have to separate components from an insurance contract, the concept of unbundling might be different under Solvency II (recent EIOPA consultation on this topic)	Medium (orange)
Recognition	For most contracts, recognition is the same. The main difference is the notion of onerous contract, specific to IFRS 17	Slight/no (green)
Level of aggregation	IFRS 17: Portfolio x group Solvency II : Entity x LoB	Significant (red)
Future cash Flows	For IFRS17 companies can leverage current Best Estimate cash flows (Solvency II, MCEV) but work will be needed to check if assumptions are reusable (contract boundaries, expenses, etc.) and granularity may be different	Medium (orange)
Contract Boundary	Broadly similar definitions to determine contract boundaries (except for e.g. Be cases: Universal Life type contracts, joint death coverage 1 year, group insurance	Medium (orange)
Expenses	Under IFRS 17, the scope of expense cash flows is different from Solvency II given the directly attributable costs, a specific treatment is also possible for acquisition costs deferred acquisition costs	Significant (red)
Discount rate	Unlike the requirements in Solvency II, there is no prescribed discount rate curve under IFRS for the determination of the discount rate. Companies should consider whether some components of SII methodology are appropriate for IFRS reporting or a new methodology is needed.	Significant (red)

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Main Similarities / Differences - 2/2

- 🔴 Significant impact
- 🟡 Medium impact
- 🟢 Slight/no impact

Item	Similarities / Differences / Nature of challenge	Impact
Risk adjustment / Risk margin	Similarities between the SII RM and the IFRS 17 RA. However, some new concepts are available for IFRS 17 (Positive and adverse scenarios, Gross of reinsurance, Excluding operational /counterparty risks, Aggregation diversification allocation, Entity vs. Group / diversification, RA at inception date, no prescribed method)	Medium (yellow)
Contractual Service Margin (CSM)	The CSM is specific to IFRS 17 and requires extensive data sets to be maintained. The CSM is measured at the opening and at the closing date.	Significant (red)
Short duration contracts	The Premium Allocation Approach (PAA) option is a simplified approach for short term contracts. There is no equivalent concept in Solvency II.	Medium (yellow)
Transition	IFRS 17: retrospective calculation Solvency II: full prospective application	Significant (red)
Presentation and disclosure	The IFRS reporting for insurance liabilities rely on Solvency II reporting like the risk disclosure. The new disclosures require additional data to support the new reporting formats.	Significant (red)
Data quality	Data availability and quality will be key for IFRS 17	Significant (red)
Reporting	Solvency II: Quantitative Reporting Templates and narrative, no P&L IFRS 17: Detailed financial statements, including a P&L	Significant (red)
Reporting period	Solvency II: Quarterly IFRS 17: Depending on the entity at least annual	Medium (yellow)

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IFRS 17 improves the stability of net income and LICAT

+ Improved
− Decreased
≈ Similar

IFRS 4 Current period net income	Impact on stability: Net income	Impact on stability: LICAT	IFRS 17 Net income & LICAT Capital treatment
New business gains	+	≈	Recognized in CSM and capital initially and amortized into net income over contract life
Investing activities	+	+	Recognized in net income and capital over asset term to maturity
Change in assumptions	+	≈	Recognized in CSM and capital and amortized into net income over contract life, or immediately into earnings if there is no CSM
Change in return assumption- ALDA & Public Equities	+	+	No longer capitalized into net income and capital at the time of change, flows through over time
Interest rate impacts and hedge ineffectiveness	+/−	+	Electing fair value through Other Comprehensive Income, therefore much of the impact is recorded in OCI and CSM. Our capital sensitivity is expected to reduce.
Other market impacts: • ALDA and Public Equities • Credit • Realized gains and losses on AFS fixed income assets	+/−	+/−	Overall variability from quarter to quarter is expected to be similar in magnitude

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3. IFRS 17 Current Challenges

IFRS 17: Current challenges and creating value beyond compliance

The year 2023 has been pivotal for those insurers adopting IFRS 17 and IFRS 9. While many insurers have focused their efforts on meeting regulatory and financial reporting deadlines to date, they are now beginning to focus on how they create value beyond compliance.

Insurers have spent significant time, effort, and financial resources on implementing IFRS 17 in areas such as accounting policy, actuarial methodologies, modeling, data, systems, or solution development. However, to truly realize value, more work is required. The key will be to take "no-regrets" steps that incorporate greater automation and adaptability.

Some of the key drivers include:

Data and technology

A fundamental shift in underlying technology and the sourcing of more granular data is necessary for reporting under IFRS 17.

Identifying, sourcing, integrating, cleansing and storing high-quality data is yet to be adequately addressed by many insurers. Insurers are also realizing that the technology they selected may require more substantial configuration and tailoring efforts than expected.

Processes, controls, and governance

The complexity of IFRS 17 means that a complete overhaul of the financial reporting process for insurance accounting is necessary.

Many insurers have already gone live with significant process and control issues, which have been compounded by prioritization, time and capacity challenges. This has led to an increase in errors, which are often being corrected via manual workarounds, and the risk of potential misstatements.

Policies and methodologies

IFRS 17 also necessitates a significant overhaul of accounting policies and actuarial methodologies.

In many cases, spurious results have required insurers to iterate policies and revise results multiple times. In other cases, some insurers are attempting to plug any remaining significant policy gaps with unsustainable workarounds.

There also remain several emerging technical issues that some insurers will need to resolve such as matters around PAA eligibility and reinsurance contracts held.

Regulatory

The level of engagement of local regulators has varied.

Some regulators have requested surveys, financial impact assessments, and/or pro forma pre- adoption financial statements. While this has pushed insurers to maintain momentum, it has also diverted resources away from core project delivery. Other regulators have been quieter, which has created uncertainty but also relieved some from additional short-term demands.

People

Resource demand has been substantial due to labor-intensive processes, manual adjustments, workarounds, and spreadsheet dependence. As a result, most insurers have reported instances of fatigue, burnout, and turnover within their teams.

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IFRS 17: Current challenges and creating value beyond compliance

01

Diving the challenges:

Faced with a daunting task, IFRS 17 implementers are grappling with several challenges, which have led to the following:

- Resource-intensive processes and longer close cycles
- Significant manual workarounds
- Data preparation and cleansing
- Large volumes of spreadsheets
- Significant process and control gaps
- High resource turnover
- Errors and potential restatements
- Regulatory risk, including non-compliance with filing deadlines

02

Preparing for the year-end audit:

Under IFRS 17 and IFRS 9, the first year-end audit will not be traditional for the following reasons:

- **Three sets of balances** within the 2023 financial statements will be subject to audit.
- **More judgments and estimates** under IFRS 17 and IFRS 9 will result in greater challenge and scrutiny from auditors.
- **Manual intervention and fluid process and controls** will generally result in auditors taking a more substantive audit approach, and may result in a greater number of control deficiencies being identified.
- **Increased use of simplifications and approximations** may lead to a greater number of items reflected in the summary of unadjusted audit differences, and potentially increase aggregation risk as it relates to materiality.

As a result, insurers will likely see greater engagement from senior members and specialists within the audit team. To succeed in the year-end audit, insurers must plan ahead and remain proactive, develop robust documentation, maintain clear and open communication with their auditors and work collaboratively with them.

03

Creating value beyond compliance:

Leaders need to set their sights on a range of different areas, which typically overlap with management's strategic priorities to create value beyond compliance. Key considerations include:

- **Automate** and **streamline** existing processes or design new processes.
- **Enhance** data management to create better business intelligence, increased accuracy in financial reporting, and the ability to identify trends and opportunities.
- **Improve** controls and governance to mitigate risks, ensure compliance, and promote better oversight.
- **Modernize** legacy systems and applications.
- **Innovate** by embracing new and emerging technologies to improve the efficiency and effectiveness of financial reporting.
- **Support** resources to avoid burnout; people remain fundamental to the path ahead for insurers.

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4. Conclusion