# IFRS17 Insurance Contracts @Generali
## Presentation to EFRAG Board

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Rome, October 10th 2017

# Agenda


I. Generali at a glance

II. Our financial reporting journey

III. IFRS 17: Overview and Areas of concern for Generali

IV. Impact assessment & Target Operating Model

V. IFRS 17 testing: Generali suggestions

VI. Conclusions

# Generali at a glance

Generali is one of the **leading insurers** in the world, offering an **extensive line of products**, with a business mix mostly exposed to **retail** and **Life**. In a nutshell:

- >60 Countries in the world
- 55 million customers
- 70 billion Euro in premiums (2016)
- 530 billion Euro of AUM
- >400 consolidated entities belonging both to EU and non-EU Countries

**Given the scale of our Group, all evaluation models set-out by IFRS 17 will be applied in a complex operational environment**

# Our financial reporting journey

## AS IS

### Current measurement models

**IFRS 4 – IAS 39**

Liabilities measured according to applicable Local GAAPs.
Financial instruments mainly at FV-OCI (with recycling).
Shadow accounting mitigates accounting mismatch

**Solvency II**

Prospective current measurement of insurance liabilities, focus on capital

**No global and consistent standard** to explain insurer performance.
**Solvency II disclosures are evolving** (beyond the Regulation) to satisfy the market needs to understand capital and cash generation

## TO BE

### Financial reporting evolution

**IFRS 17 – IFRS 9**

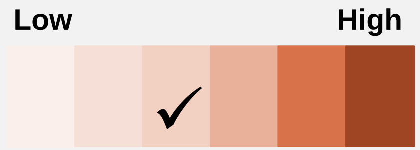
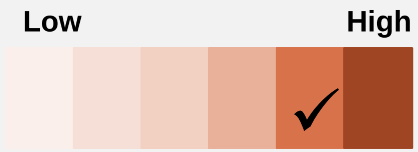
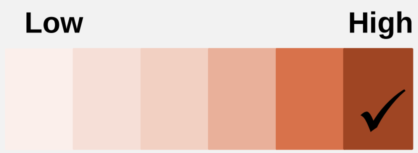
Prospective current measurement of liabilities (expected different from SII).
Financial instruments mainly at FV-OCI.
**New income statement**

**Solvency II**

Prospective current measurement of insurance liabilities, focus on capital

**IFRS 17** is a fundamental change in financial reporting and it should become the **reference metric to explain the performance of insurers**

# IFRS 17: Overview of measurement models

| Generali's business examples | Eligible measurement model | Expected applicability of the measurement model to our business |
|---|---|---|
| • Multi-year P&C<br>• Protection business<br>• All other saving products not eligible for VFA models | **General Model**<br>**Default model for all insurance contracts** |  |
| • Most of P&C business (both Motor and Non-Motor) with duration <=12 months | **Premium Allocation Approach**<br>**Optional simplified model for short term contracts with little variability of cash flows** |  |
| • Traditional saving business run by EU-based entities. As a preliminary estimate, >80% of Italian, German and French Life technical provisions are eligible for the VFA approach<br>• Unit-linked business | **Variable Fee Approach**<br>**Model for direct participating business** |  |

# IFRS 17: Areas of concern 1/3

## Pooling risks and portfolio management

- A large number of contract issued reduces the insurer's risk of incurring in a loss thanks to the pooling risk mechanism
- For certain participating policies the profit sharing is based on an intergenerational mutualization of contracts written in different years but sharing the same pool of assets

Financial reporting should reflect the level of aggregation that is relevant for **managing and steering the business**

- **L&H:** **annual cohorts requirement** (for instance in Italy, Germany and France) **is not reflecting the intergenerational mutualization of participating policies leading to artificial and costly reallocation of mutualised business into annual groups**. Allowing for intergenerational grouping is not in contrast with the recognition of onerous contracts in case of for loss making business written. In addition, roll-forward disclosure of CSM separates new cohorts contribution from the in-force book
- **P&C:** **a top down grouping** based on **current internal financial information** is workable. Excessive granularity based on a bottom up approach would result in an operational burden, change in pricing strategy and potential social impacts with no tangible benefits for the users

# IFRS 17: Areas of concern 2/3

## Performance reporting

With IFRS 17 P&L will be mainly affected by:

- **Differences between actual and expected cash flows** related to current, or previous, reporting periods
- **Release of the risk adjustment** based on the expiration of non-financial risks
- **Release of the CSM** based on coverage units

While the first 2 components of financial performance properly reflect relevant drivers of the financial performance of an insurer, the release of CSM using the coverage units method might improperly reflect actual emergence of profits

**Coverage units approach need to be tested** in practice

- The **risk**, **especially for VFA business, is to disclose a linear profit pattern:**
  - Inability to connect with the internal analysis of profit by source used for business steering
  - Lack of connection with cash flow generation: **key priority for our investors!**
  - We would like to test alternative amortization drivers, better linked with the investment management service and the expected recognition pattern of the variable fee

# IFRS 17: Areas of concern 3/3

## Volatility and accounting mismatch

- **Financial statements** shall **reflect** reliably the **risks mitigation strategies** (reinsurance and hedging) used by the entity, both for insurance and financial risks
- Economic mismatch shall be reflected, while artificial volatility due to accounting mismatch needs to be avoided

- **VFA model** fit for purpose since it **neutralizes P&L volatility**, if a sensible level of granularity is allowed
- **IFRS 9 leads to additional P&L volatility** on P&C and other Life contracts due to classification of equity-type and structured instruments. No hedging solution for business outside of VFA
    - Potential unwanted change in asset mix and ALM strategy
- **Reinsurance:** possible mismatch between direct and ceded business and reinsurance issued and held due to different measurement models, CSM treatment at inception, recognition criteria and differences in contract boundaries

# Impact assessment – Main Findings & Challenges

We had a preliminary assessment of the IFRS 17 requirements along four different dimensions: data, people, processes and systems. Impacts were evaluated both at a parent company and at a pilot subsidiaries

## Data

- **Data granularity** for grouping management
- Management of **non-distinct investment components**
- **Transition** (historical data); full retrospective unrealistic
- **Data quality** issues

## People

- **Workforce staffing** and **skills** to be enriched to properly manage new financial reporting
- **Integration** between actuarial and accounting people/skills
- **Several functions** to be trained and involved due the impact on their business as usual

## Processes

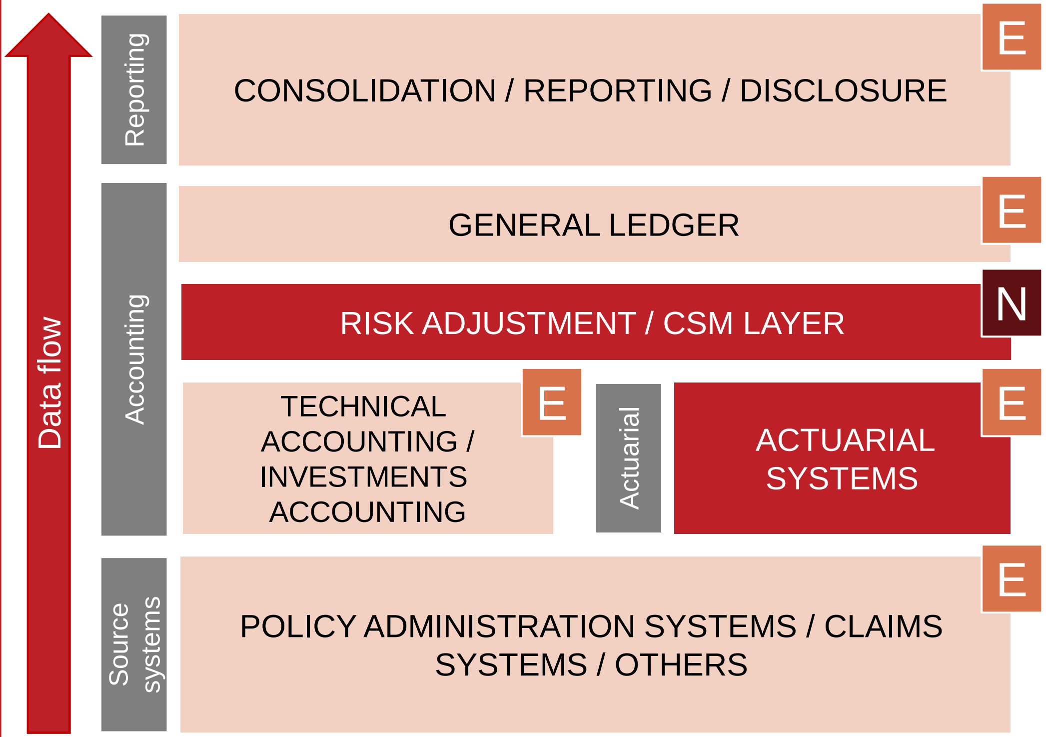
- **Timing: acceleration** in order to meet current reporting deadlines despite the higher complexity
- Increased valuation **frequency** for business steering and external disclosure

## Systems

- **New calculations** (e.g. CSM) require **new IT systems**
- **Interfaces** between actuarial and accounting to be enhanced or created
- **Current actuarial platform needs to be enhanced or changed due to** the higher granularity and the different requirements compared to Solvency II and MCEV

# Impact assessment – Impacts on System architecture

## Illustrative IFRS17 application architecture




- **Large number of systems** impacted
- As per today **no IT end-to-end solution exists** and offering is still **not mature. Lack of skilled resources for the implementation**
- Granularity and accuracy needs are more demanding than Solvency 2, **investments on actuarial platforms** likely to be very substantial
- Opportunity to **standardize and centralize** closing processes

***Legenda*** Impact: High | Medium — Type of intervention: E nhancement | N ew module

# Target Operating Model

## Design of the new Target Operating Model

- New **process and IT architecture**
- Review of **service delivery model** (e.g. global vs local responsibilities)
- Evaluation of **organizational impacts** at a Group and Local level

## Main drivers for development

- **Leverage on Solvency II investment** unless explicit benefits are coming from a different approach
- New level of **interaction between accounting and actuarial functions**
- **New professional profiles** on accounting and management control and steering roles, which shall require an actuarial expertise
- **Communication** with external stakeholders to get familiar with the new model, when possible

# IFRS 17 testing: Generali suggestions

## EFRAG case study

**Comprehensive testing is important in order to assess the appropriateness of the standard.** This must be done thoroughly and comprehensively due to profound ranging impact on industry.

**We propose a two phases approach:**

### First phase by 1H 2018 with focus on

- **Selected types of insurance contract portfolios**, including interactions with **IFRS 9**
- Quantitative testing of **specific critical technical areas** of the standard **applying sensitivities** to the results

### Second phase by the end of 2018 trying to achieve

- More **comprehensive view of balance sheet and income statement**, including **stress scenarios**
- **Deeper assessment** of any issues identified in phase 1
- Analysis of any **new inputs coming from TRG** process that is expected to use all 2018

The **proposed approach** has the **advantage** of:

- pointing out any **technical issues** at an early stage of the endorsement process
- considering the **broader impact of the standard** and the potential challenges it may arise when using it for reporting and explaining our performance to the market as well as the impact on products and potentially policyholders

# Conclusions

1 IFRS 17 is a very significant step towards a **greater transparency and comparability** across our industry

2 **To ensure its success, some key elements of IFRS 17 need to be further explored** together with the key stakeholders (auditors, users, etc.) and leveraging the IASB/TRG process as well

3 As was the case with Solvency 2, it is important to **test appropriately the new standard before its application**

4 **EFRAG will play a key role via the endorsement process. Generali is fully committed to supporting this process** and achieving the best possible outcome for the industry and all users