

13 June 2018

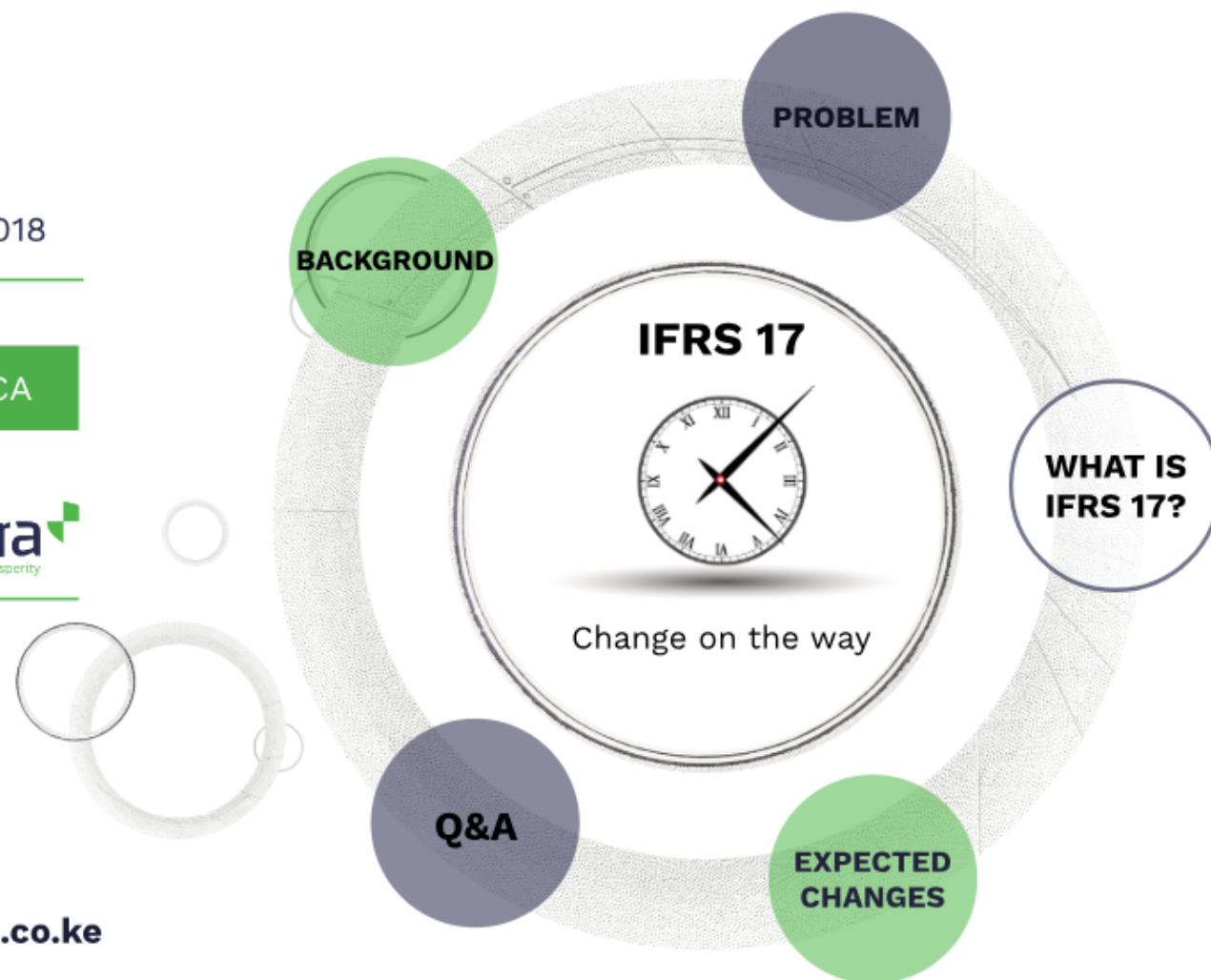
**Seth Chengo**

FIA, FCCA

**zamara**  
Powering Prosperity



**schengo@zamara.co.ke**





**WHY AND  
WHY NOW?**

## **BACKGROUND**

---

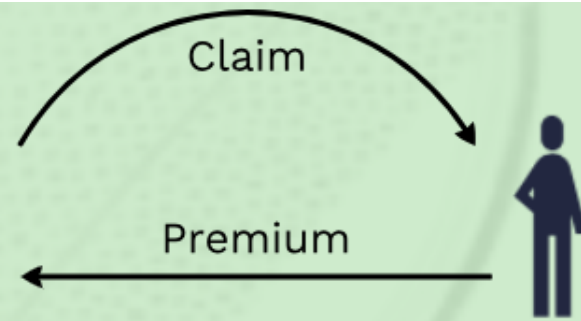
**WHY?**


**WHY  
NOW?**

# WHY AND WHY NOW?

1 It's a trust business

2 When kingdoms fall

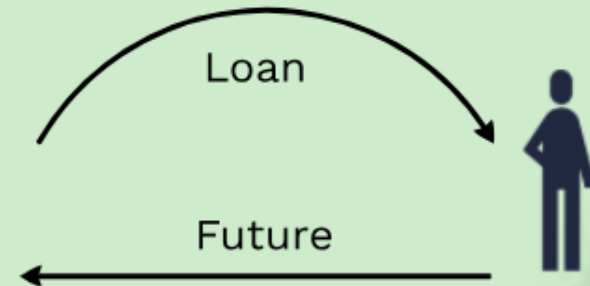
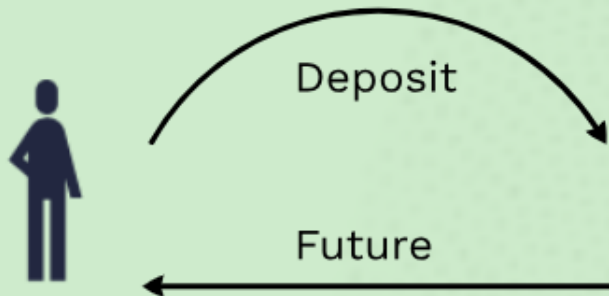


Insurance 

Banking 

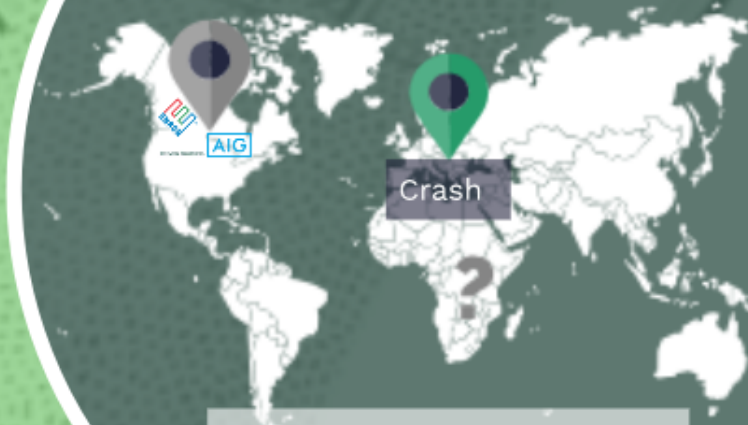
# WHY?

It's a trust business



## WHY NOW?

### When Kingdoms Fall



You can't control what  
you can't measure

An assessment of 640 failed US  
companies between 1969 and 1998

Primary Causes	Number of Companies	% of Total Identified
Insufficient Reserves	145	34%
Rapid Growth (Under Pricing)	86	20%
Alleged Fraud	44	10%
Overstated Assets	39	9%
Catastrophe Losses	36	8%
Significant Change in Business	28	7%
Impaired Affiliate	26	6%
Reinsurance Failure	22	5%
Total Identified	426	100%

Source:  
A.M.Best

13 June 2018

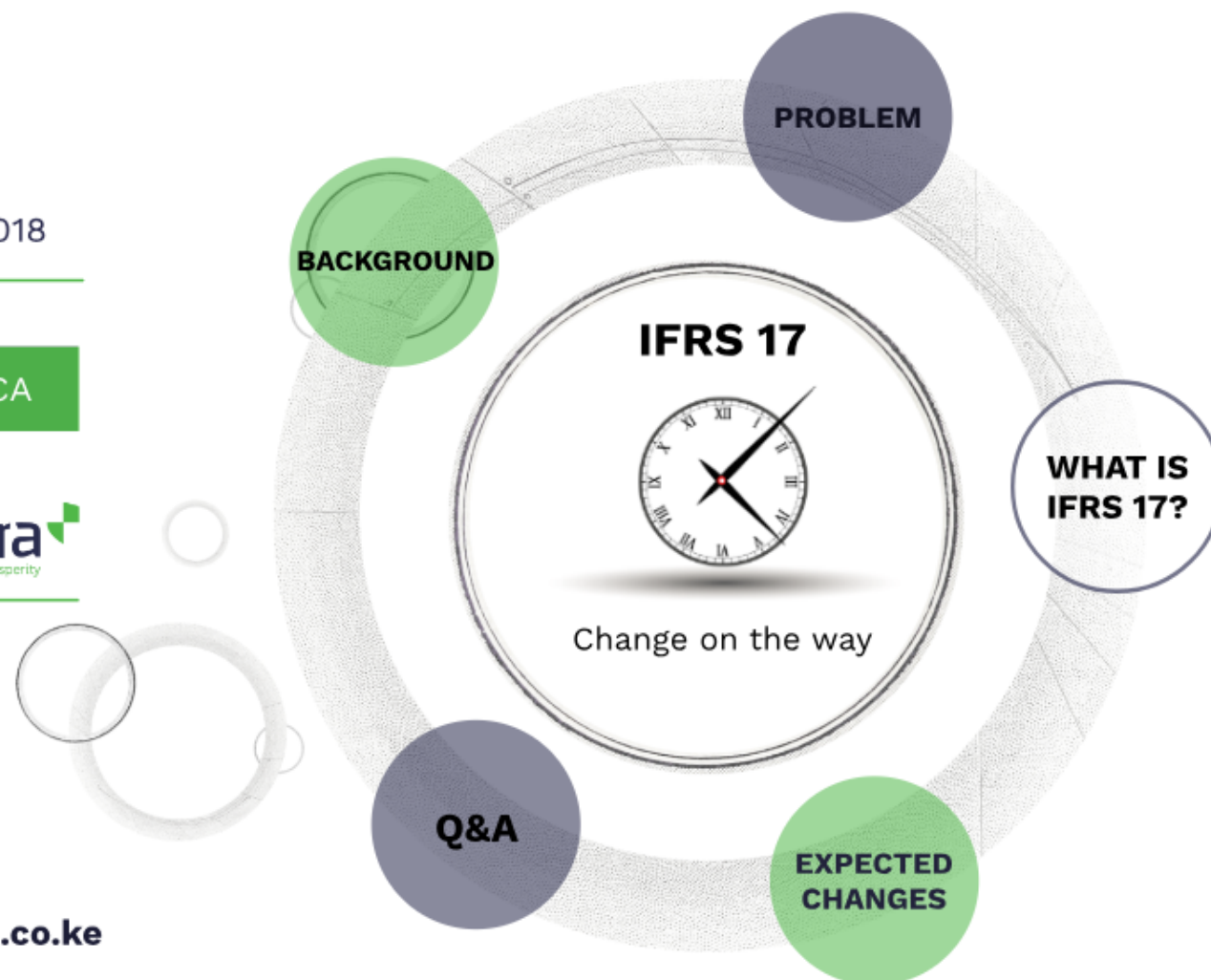
**Seth Chengo**

FIA, FCCA

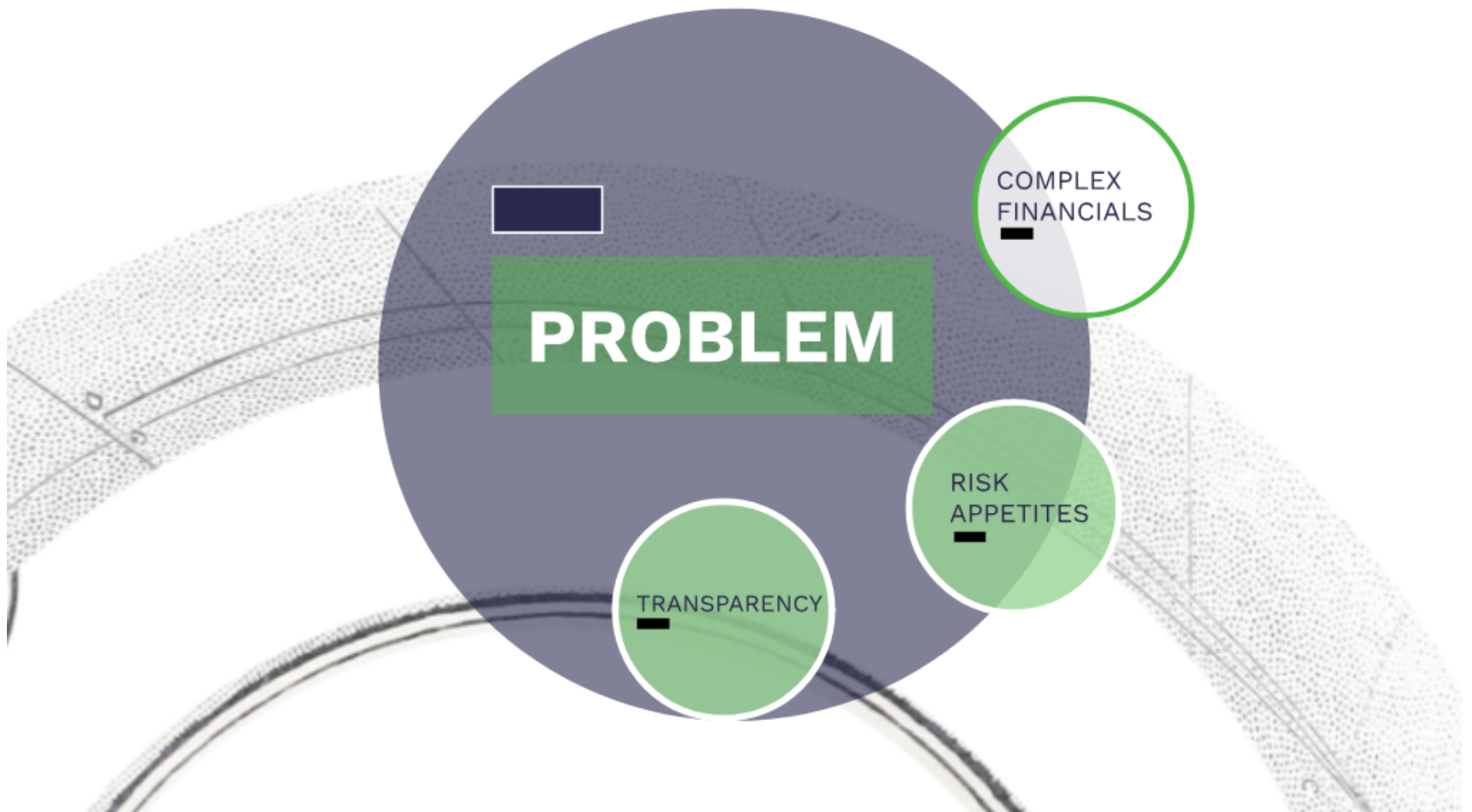
**zamara**  
Powering Prosperity



**schengo@zamara.co.ke**







# COMPLEX STATEMENTS

One/two Contracts....  
.... different disclosures

## Liabilities

Actuarial Long Term Liabilities  
Outstanding claims reserve  
Unearned premium  
Payables arising from reinsurance arrangements  
Tax payables  
Other payables  
Borrowings

\_\_\_\_\_  
Total Liabilities  
\_\_\_\_\_

## Liabilities

Actuarial Long Term Liabilities  
Outstanding claims reserve  
Unearned premium  
Payables arising from reinsurance arrangements  
Tax payables  
Other payables  
Borrowings

\_\_\_\_\_  
Total Liabilities  
\_\_\_\_\_



# COMPLEX STATEMENTS

One/two Contracts....  
.... we're not done yet!

## Assets

Property and equipment  
Intangible assets  
Goodwill  
Investment property  
Investment in property funds  
Quoted ordinary shares at fair value through other comprehensive income (OCI)  
Financial assets at fair value through profit or loss  
Government Securities at amortised cost  
Corporate Bonds at amortised cost  
Mortgage loans and receivables  
Loans and receivables to policyholders  
Reinsurance arising out of reinsurance agreements  
Reinsurance arising out of direct insurance agreements  
Reinsurer's share of insurance liabilities  
Deferred acquisition costs  
Deferred income tax  
Current income tax  
Other receivables  
Retirement benefit asset  
Investment in liquid funds  
Deposits with financial institutions  
Cash and bank balances

---

Total Assets

---

# COMPLEX STATEMENTS

One/two Contracts....  
.... we're not done yet

## Assets

Property and equipment  
Intangible assets  
Goodwill  
Investment property  
Investment in property funds  
Quoted ordinary shares at fair value through other comprehensive income (OCI)  
Financial assets at fair value through profit or loss  
Government Securities at amortised cost  
Corporate Bonds at amortised cost  
Mortgage loans and receivables  
Loans and receivables to policyholders  
Reinsurance arising out of reinsurance agreements  
Reinsurance arising out of direct insurance agreements  
Reinsurer's share of insurance liabilities  
Deferred acquisition costs  
Deferred income tax  
Current income tax  
Other receivables  
Retirement benefit asset  
Investment in liquid funds  
Deposits with financial institutions  
Cash and bank balances

---

Total Assets

---

# RISK APPETITES

## Company A

Booked claim reserve  
=  $100\text{m} * 0\%$   
= 0 (liability)

IBNR (simple example)  
= % of Booked claim  
=  $20\% * 0$   
= 0 (additional liability)



## Company B

Booked claim reserve  
=  $100\text{m} * 25\%$   
= 25m (liability)

IBNR (simple example)  
= % of Booked claim  
=  $20\% * 25\text{m}$   
= 5m

# TRANSPARENCY

## Company A

- Strong tail assumed
- Correct loss ratios
- Historical prudence

## Company B

- Poor data
- Weak assumptions
- Historical leaniance

Notes to the accounts for both:  
Chain Ladder method selected

13 June 2018

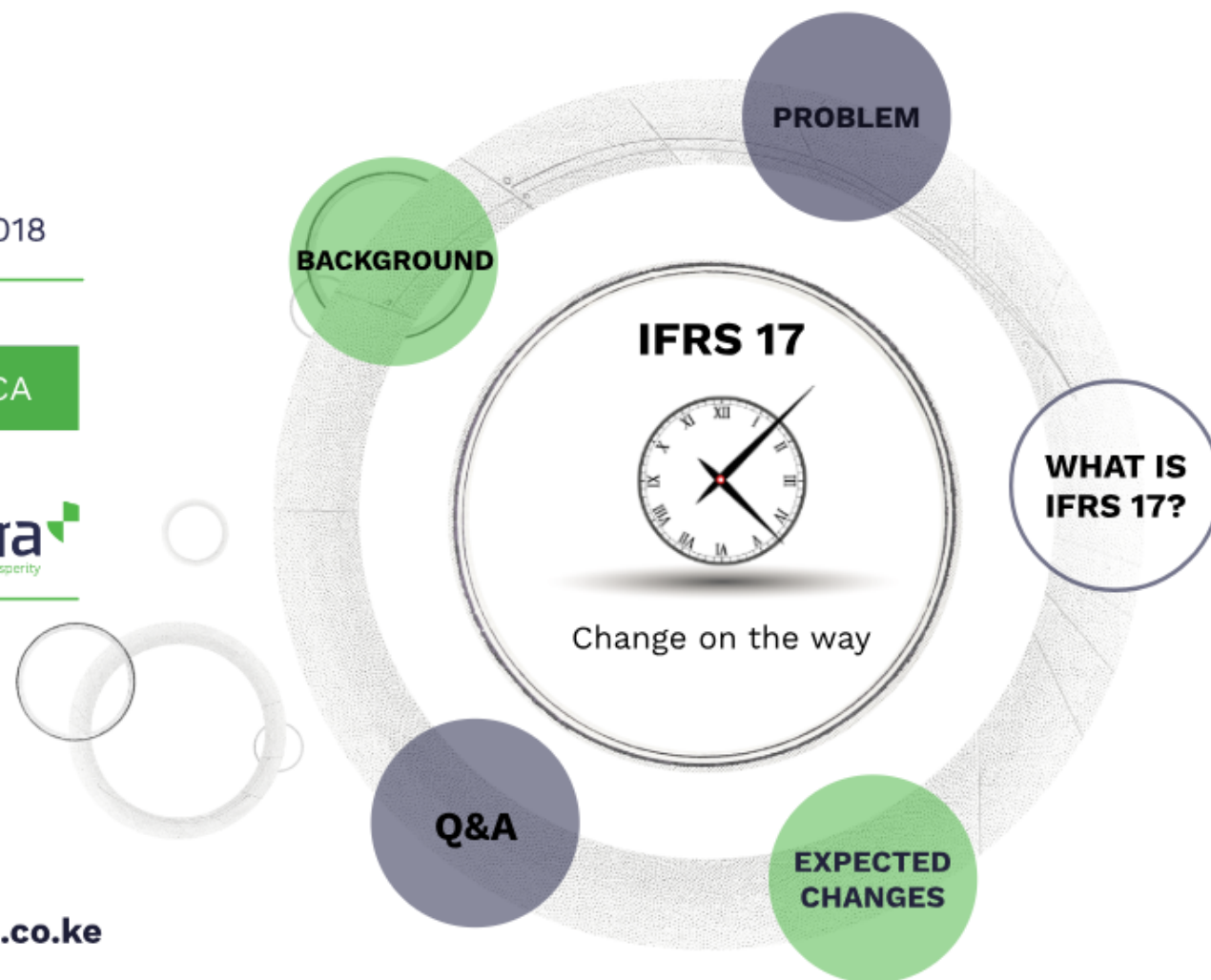
**Seth Chengo**

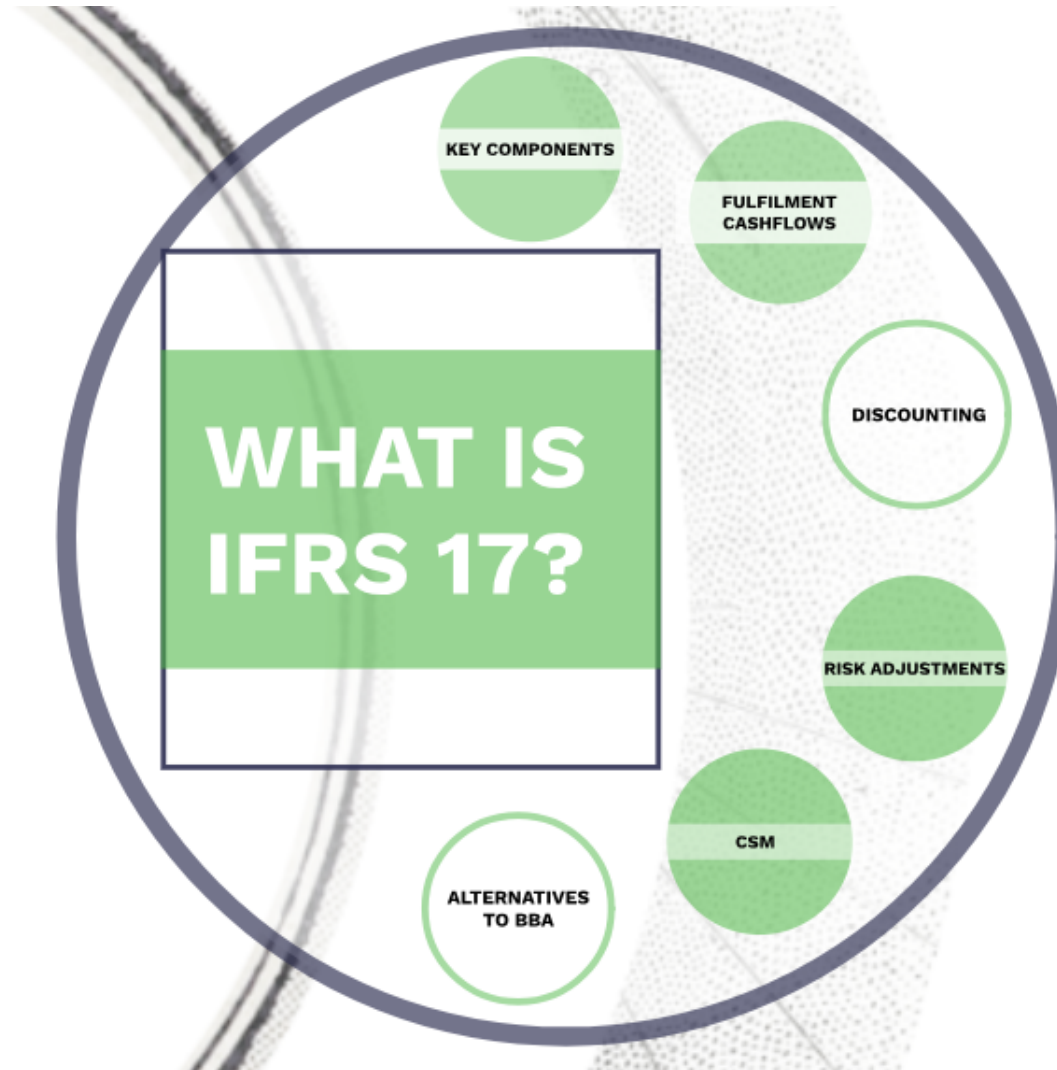
FIA, FCCA

**zamara**  
Powering Prosperity



**schengo@zamara.co.ke**

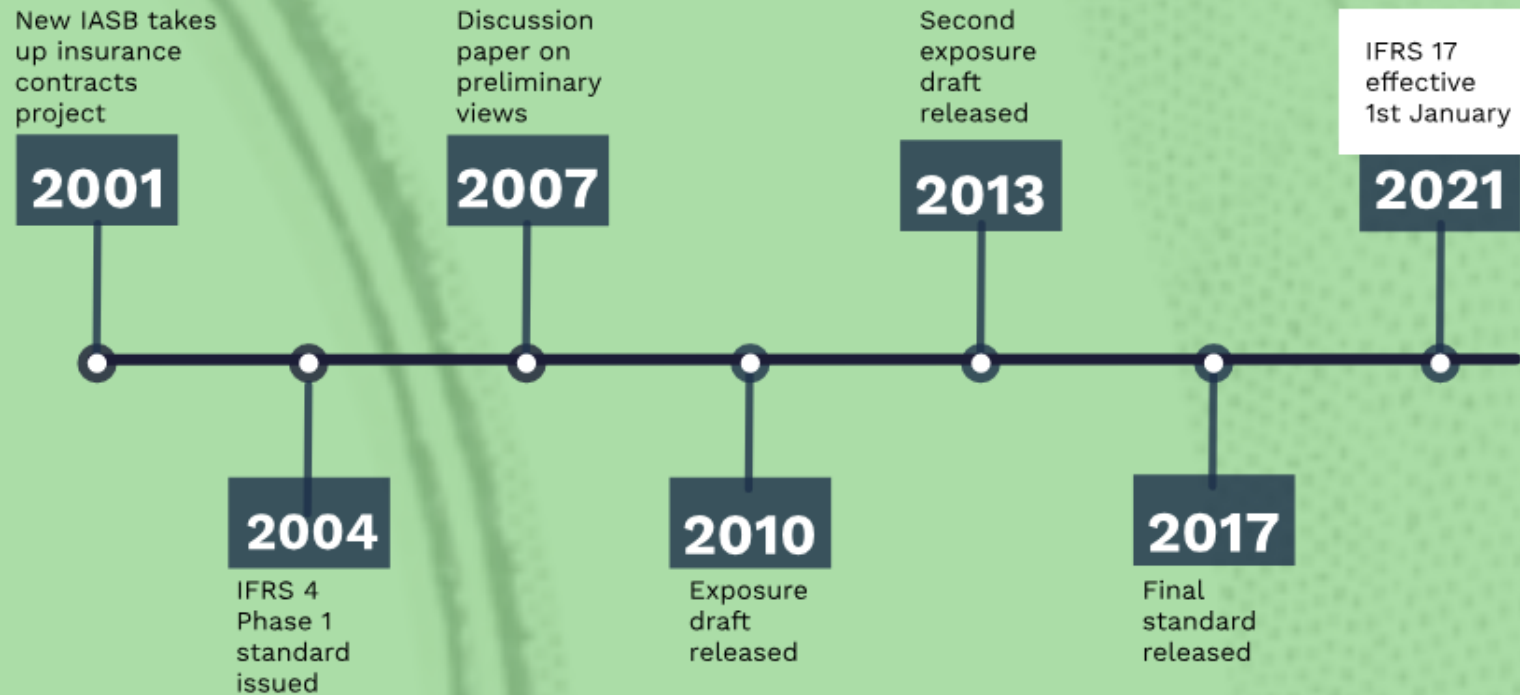






# HISTORY OF IFRS 17

## TIMELINE





## Building Block Approach (BBA)

General Measurement Model  
(GMM)

Contractual Service Margin

Risk Adjustment

Discounting

Fulfilment cashflows

# FULFILMENT CASHFLOWS

The cashflows shall take the following into account:

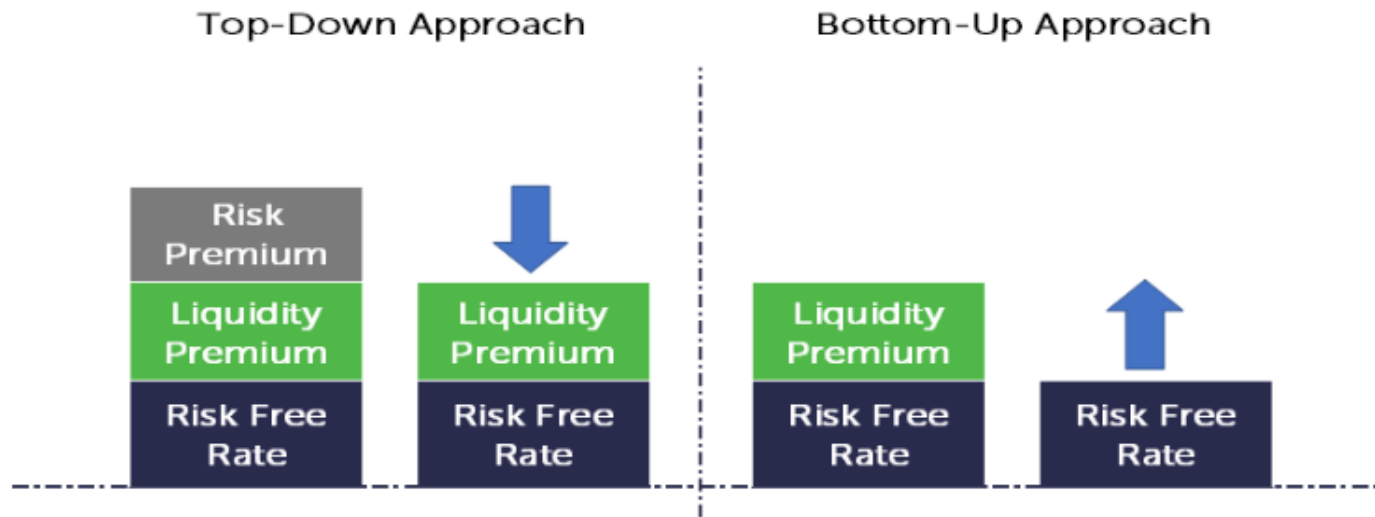
- Incorporate the timing, amounts and **uncertainty** of the cashflows
- The cashflow estimates shall reflect the conditions **existing at the measurement date**

Typical cashflows within the boundary of an insurance contract:

- Premiums and claims
- Acquisition costs
- Policy administration and maintenance costs
- Reinsurance cashflows
- Profit commissions
- Etc

The cashflows may also be estimated a higher level of **aggregation** and allocated to the individual groups of contracts

# DISCOUNTING



The discount rate applied shall reflect the time value of money, the timing, currency and liquidity of cashflows underlying the insurance contracts and be market consistent.



# **RISK ADJUSTMENTS**

# Approaches & Disclosures

Risk adjustment is the compensation that the entity requires for bearing uncertainty about the timing and amount of cashflows



Cost of Capital



Confidence Level



Conditional Tail Expectation

Salary Option 1: \$100 per month

Salary Option 2: an average of \$100 on average every month

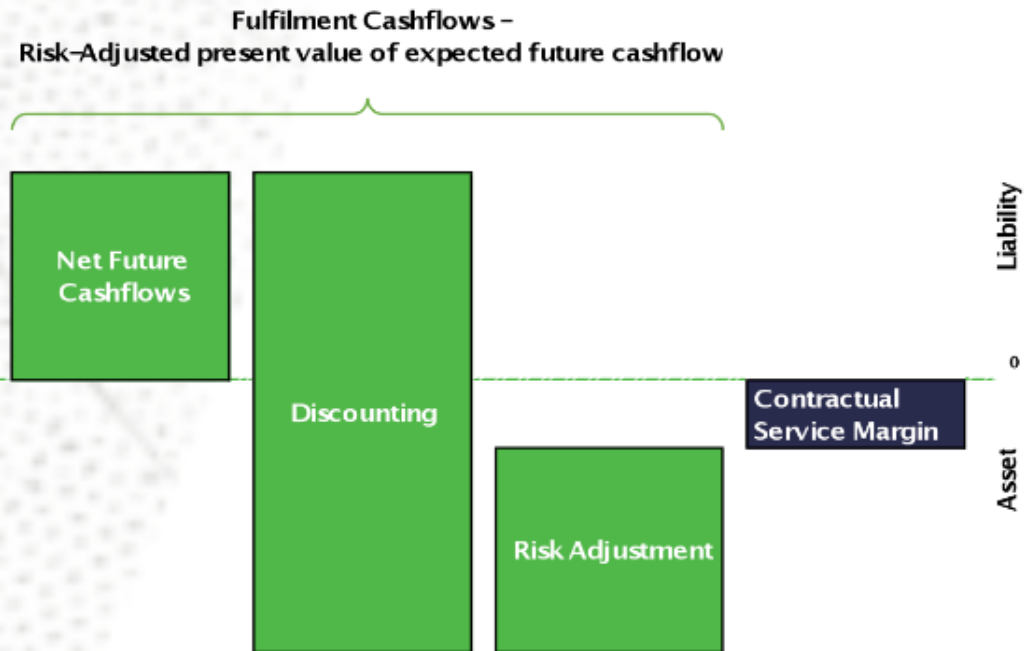


# **CONTRACTUAL SERVICE MARGIN (CSM)**

# CONTRACTUAL SERVICE MARGIN

## Profitable Groups:

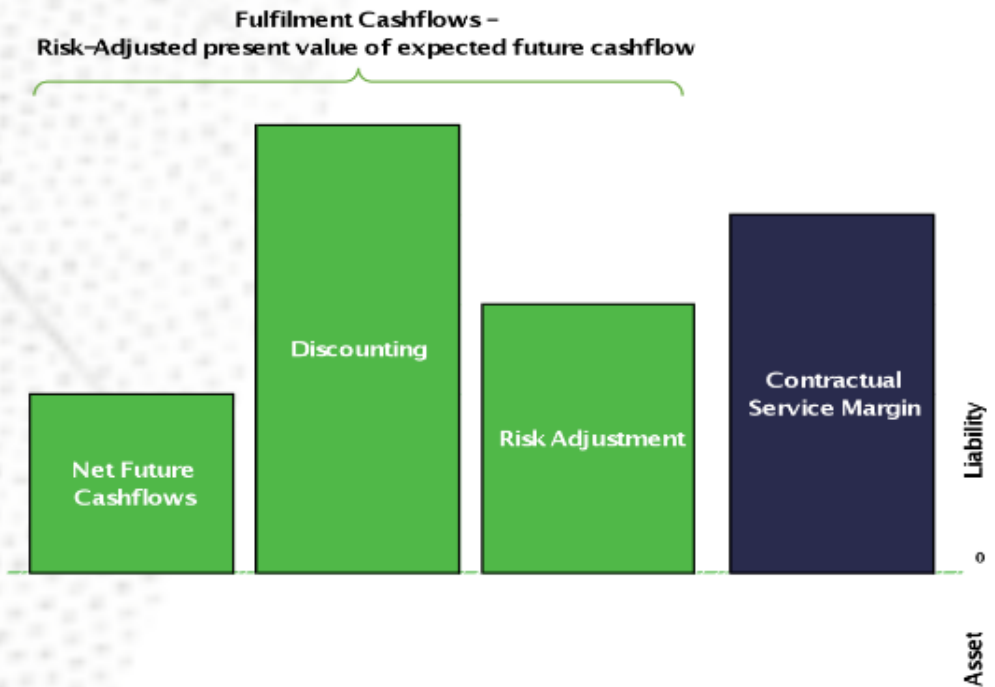
- Positive fulfilment cashflows
- CSM represents unearned profit for profitable groups
- **There is no gain on initial recognition of the group i.e. no day 1 profits**



# CSM FEATURES

## Unprofitable Groups:

- Negative fulfilment cashflows
- CSM represents a loss
- A loss will be recognised at initial recognition



# ALTERNATIVES TO BBA

## Premium Allocation Approach

Closer to existing models for unexpired risks.

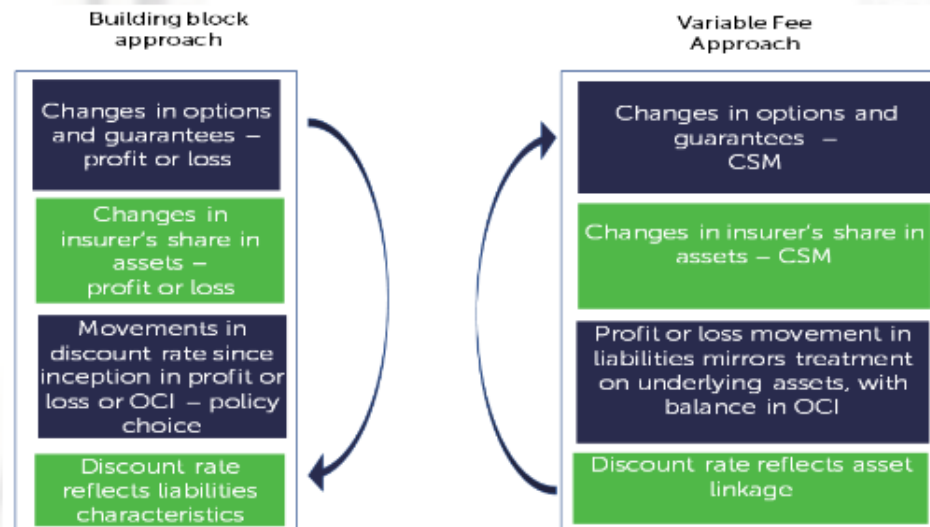
Also applicable to short-term life insurance contracts such as Group Life contracts.

For multi- year contracts, judgement required on whether significant differences will exist if BBA model is applied.

	Unexpired Risks	Expired Risks
Premium Allocation Approach (PAA)	Premium Liabilities UPR less DAC	Discounted Value of Fulfilment (Future) Cashflows
		Risk Adjustment

# ALTERNATIVES TO BBA

## Variable Fee Approach



The variable fee approach considers the variable fee associated with direct participating contracts.

13 June 2018

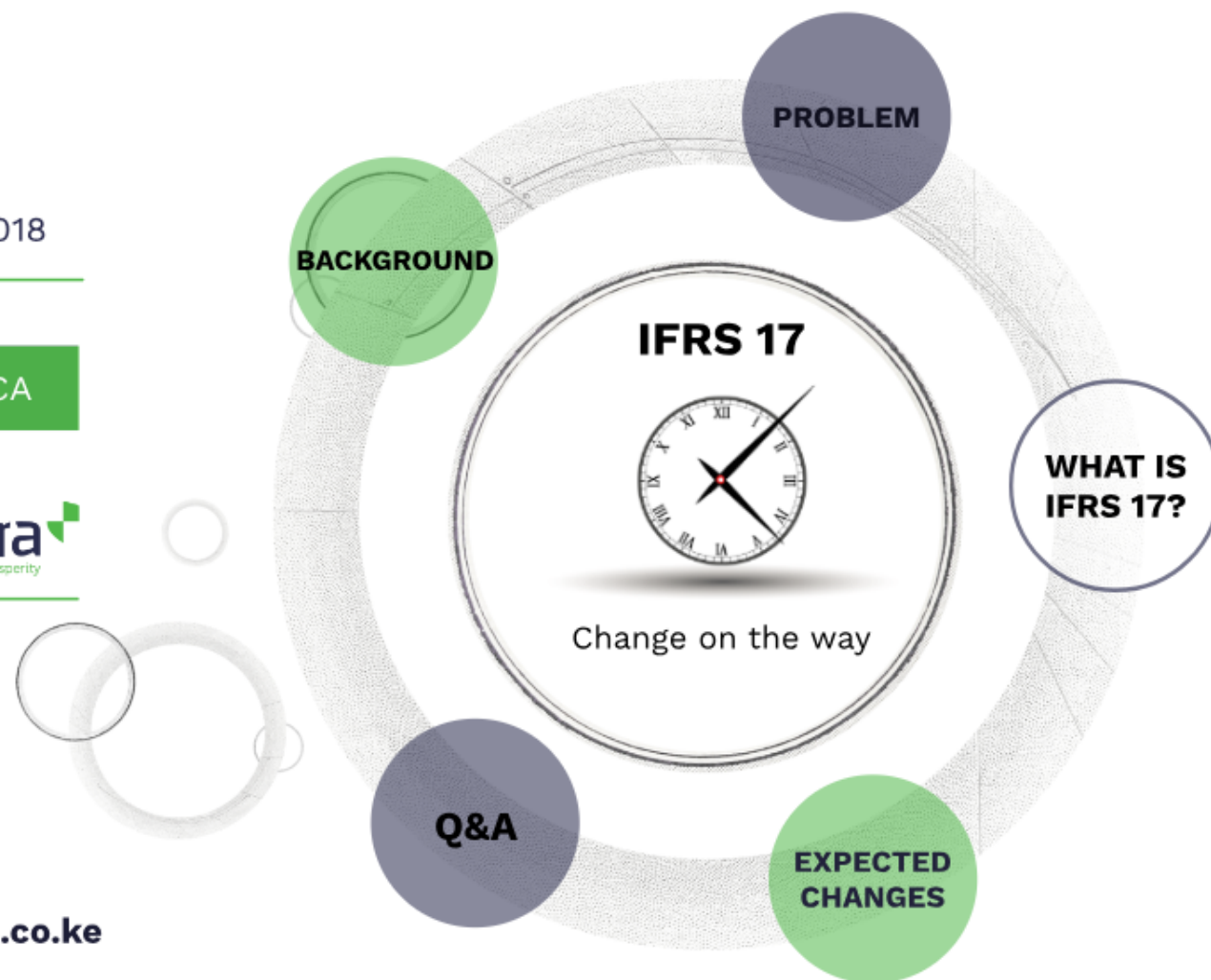
**Seth Chengo**

FIA, FCCA

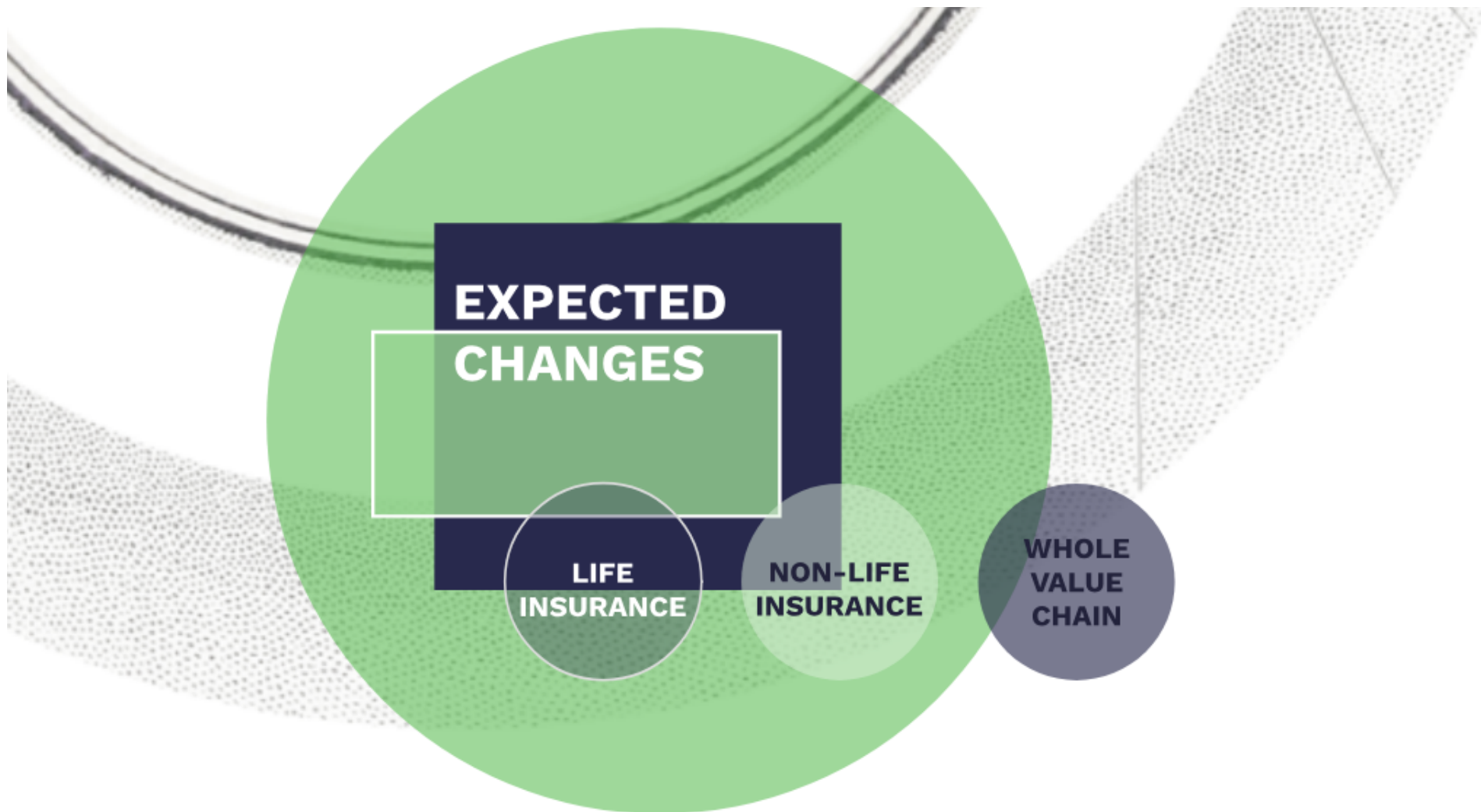
**zamara**  
Powering Prosperity



**schengo@zamara.co.ke**







# LIFE INSURANCE



Significant accounting  
changes are expected

IMPACT

# LIFE INSURANCE

## IMPACT

- Using current estimates
- Disaggregating changes in remaining liability
- Tracking the CSM at a group level

# NON-LIFE INSURANCE



Accounting may have  
similarities to current  
practices

IMPACTS

# NON-LIFE INSURANCE

## IMPACTS

- Qualifying for premium allocation approach
- Discounting of incurred claims
- Onerous contracts

# RISK APPETITES

---



UK  
Vehicle Value - \$10,000



Premium - \$2,000



# RISK APPETITES

---



UK  
Vehicle Value - \$10,000



Kenya  
Vehicle Value - \$20,000



Premium - \$2,000

Premium - ?

Premium - \$800

## Additional Risks



# WHOLE VALUE CHAIN



No more business  
as usual



# WHOLE VALUE CHAIN IMPACT AREAS

---

Mergers and acquisitions

Investment policy

Distribution strategy

Executive compensation

**Reinsurance strategy**

Costs and cost allocation

Product design and pricing

13 June 2018

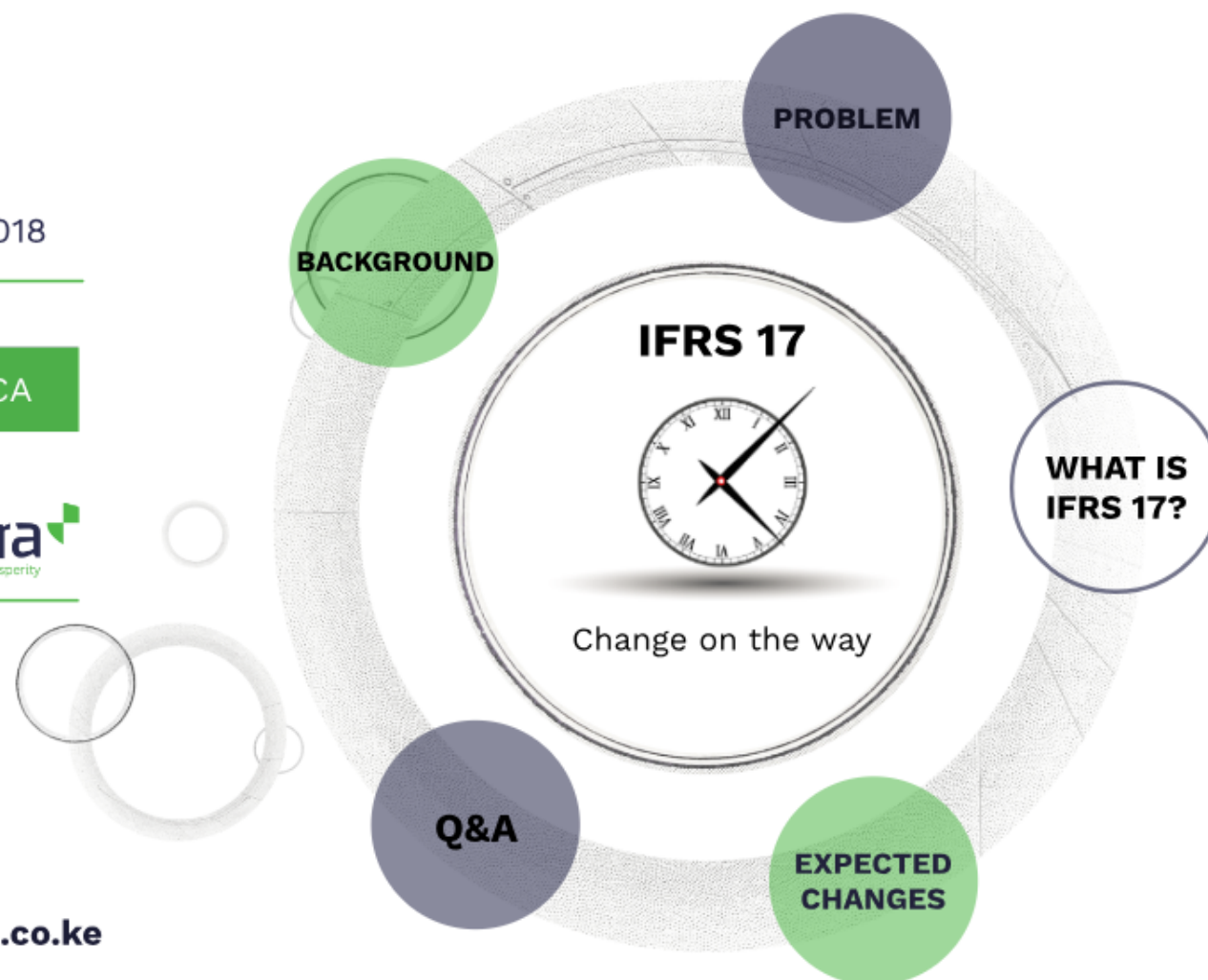
**Seth Chengo**

FIA, FCCA

**zamara**  
Powering Prosperity



**schengo@zamara.co.ke**



# CONCLUSION

## The issues are

Globalisation of operations  
Complex statements  
Different risk appetites  
Lack of transparency

## IFRS 17 aims to:

Improve comparability  
Simplify face of accounts  
Converge approaches  
Improve transparency in disclosures

# Q & A

**Seth Chengo, FIA FCCA**  
**[schengo@zamara.co.ke](mailto:schengo@zamara.co.ke)**



13 June 2018

**Seth Chengo**

FIA, FCCA

**zamara**  
Powering Prosperity



**schengo@zamara.co.ke**

