

# IFRS 17 and its impact on Takaful

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## Introduction

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# Takaful and IFRS 17

Peter Casey

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Structures of modern takaful

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## Why takaful?

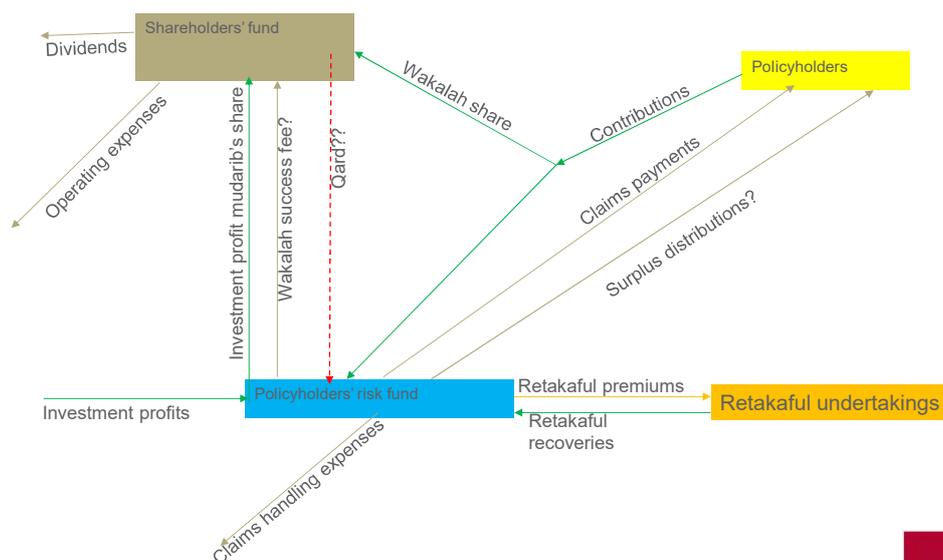
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- Shari'ah issues around trading in risk
- Good Shari'ah basis for mutual guarantee and mutual assistance
- Most straightforward version of takaful would be pure mutual (as in Sudan) – but very difficult to found a new mutual
- So most modern takaful companies have one or more policyholder funds embedded in a shareholder company
- No standard model - and different approaches in Saudi Arabia and Iran

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## A general takaful model (hybrid)

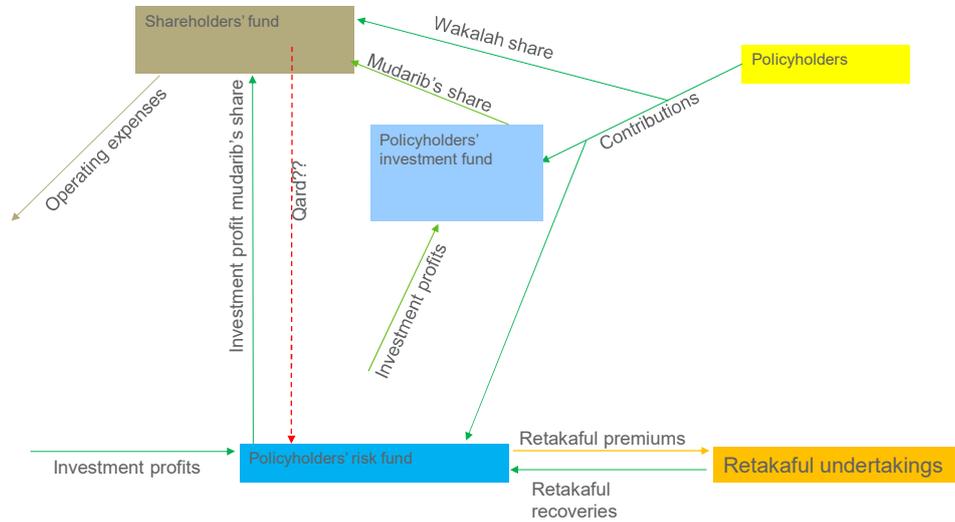
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## A life (family) takaful model (hybrid, simplified)

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## Policyholders' Investment Fund

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- Generally functions rather like unit-linked policies
- No bonuses or similar discretionary elements
- But may “drip feed” Policyholders' Risk Fund

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## Takaful and IFRS 17 – some issues

## Is takaful insurance?

- Argument against is “risk sharing versus risk transfer”

But ...

- AAOIFI Shari’ah standards and OIC Fiqh Academy both refer to “Islamic insurance”
- A takaful contract does transfer risk between two legal persons
- Purest form of takaful would be a mutual, and no doubt that conventional mutual is undertaking insurance
- If not insurance, then would not be eligible for compulsory covers

## Takaful and IFRS 17: the good news

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- Relatively simple products
- Very limited use of derivatives/hedging features
- Discretionary features largely confined to surplus distribution from PRF
- Relatively simple investment programmes (so IFRS 9 less problematic than for banks)

## Structure of funds

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- IFRS 17 based on legal entity
- But funds have different “ownership” and therefore fund-level disclosures are appropriate
- Fund level solvency regulation – and alignment of accounting bases
- Where is insurance risk being taken?
- Some cashflows (e.g. claims) fall against PRF. Others (e.g. acquisition costs) against SHF.
- Correct attribution of other flows (e.g. retakaful)

## Transfers between funds

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- How to account for (e.g.) wakalah fees, wakalah success fees, mudarib's share – bearing in mind that structures may differ
- The problem of qard (or other support):
  - When it must be paid
  - How to account for possibility before payment
  - How to account thereafter
- Surplus distributions a regulatory but also an accounting problem

## The lessons from IFRS 9 in Islamic banks

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- Many have limited capacity and rely on their regulators to tell them what to do
- But insurance regulators generally have less capacity than banking regulators
- Some banks used AAOIFI standards for guidance, even in IFRS jurisdictions
- But AAOIFI standards came well after IFRS 9
  
- And Insurance Capital Standard is on its way



# Thank you

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## Applying IFRS 17 on Takaful

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30 September 2019



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# 1

## Overview of IFRS 17

## Overview of IFRS 17

### Objectives of the standard

- Single measurement approach for similar insurance contract liabilities and revenue, allowing **greater comparability** amongst insurance companies
- Insurance contracts **measured at current value** and estimated future payments will be reported on a **discounted basis**
- Information about different **components of current and future profitability** will be provided
- **Revenue** will reflect provided **insurance coverage**

### Key highlights

- A more complex measurement model under IFRS 17 introduces **greater levels of system complexity and cost**
- Changes to **financial statement presentation** will drive new key performance indicators and MI requirements
- Enhanced disclosures requirements will **increase transparency of reserve adequacy and quality of earnings**

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## Why is IFRS 17 a big deal? It's harder than it looks...

Company's can't move forward because the Standard is not final...

**No! - the issues are understood and many decisions can be made now**

### Debunking myths!

No one is the same...

**Products, systems, data, processes, markets, stakeholders all differ**

It's an accounting standard so it's a finance problem...

**No! – it will impact all, including future strategies!**

We only write short term business so it does not impact me!

**No! – we are finding data challenges, process changes etc that require systems and process changes**

Dependencies – organisations do not stand still and changes are a fact of life.

**How do you integrate IFRS 17 into ongoing changes? ERP systems, new products, markets etc...**

It's not due until 2022. There's plenty of time...

**2022 is closer than you think**

We can utilise our current systems and data storage

**IFRS is very different to current standard**

We can just employ some contractors to get the work done

**What is your IT strategy?**

We have all of the data we need for IFRS 17

**Data quality is key**

I'm a General Insurer. We can just use the PAA approach. It will be simple

**PAA is only the beginning!**

Will it impact Takaful business?

**Yes – IFRS 17 is an accounting standard**

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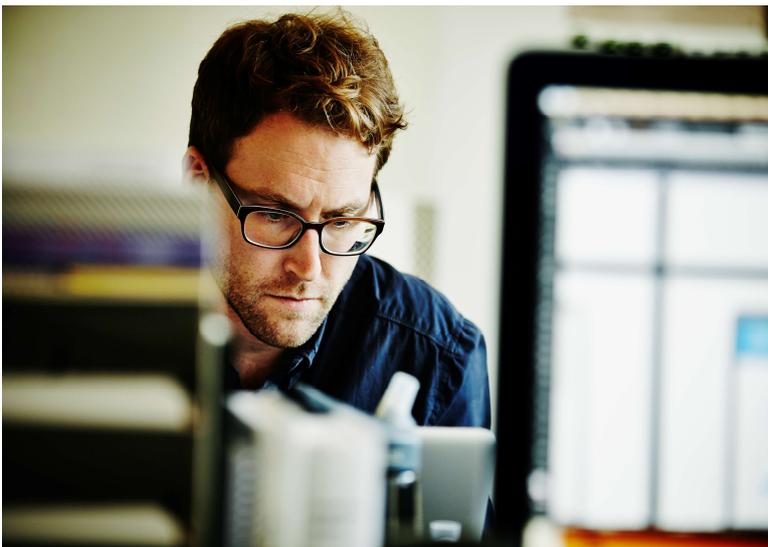
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## Approaches to apply IFRS 17 to Takaful

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### Is applying IFRS 17 to Takaful contracts Shariah compliant?



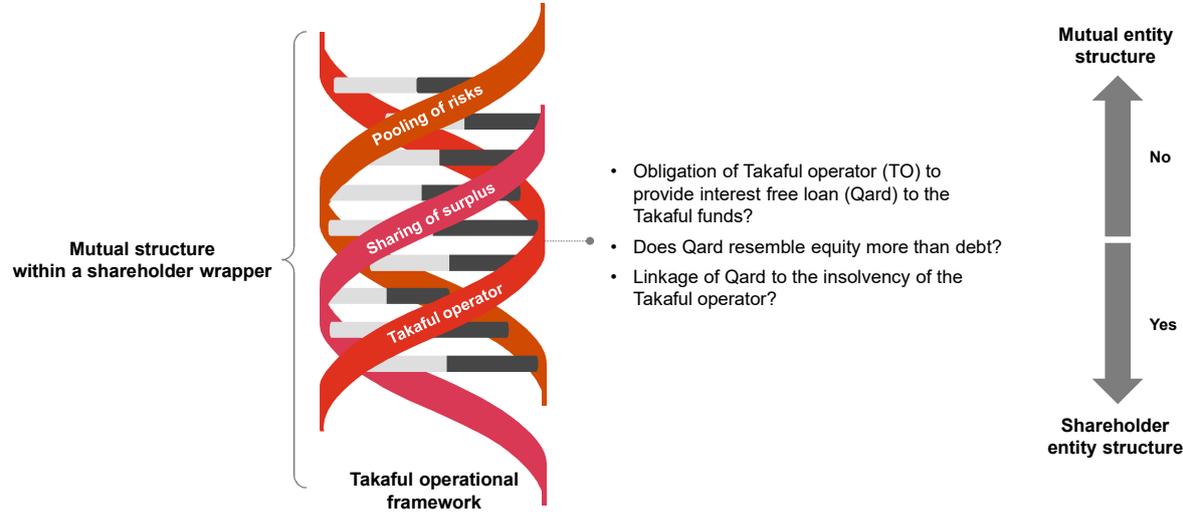
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- IFRS 17 standard establishes principles for the recognition, measurement, presentation and disclosure of insurance contracts issued.
- IFRS 17 does not change the nature of insurance business as it does not drive the product structure or terms & conditions of insurance contracts.
- Takaful players in various countries are already applying IFRS 4 or equivalent to prepare the financial statement.

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# Transfer of insurance risk from the Participant to the Takaful Operator?

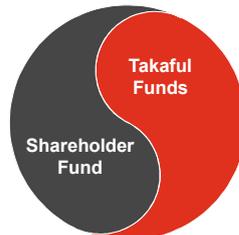


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# Two possible structures for applying IFRS 17 to Takaful



Takaful operator is a manager of risks and Takaful funds



Strong economic relationship between a Takaful operator and the participants' funds

<b>Application of IFRS 17</b>	Takaful entity as a mutual insurance entity	Takaful entity as a conventional with-profits insurer
<b>Additional disclosures</b>	Shareholders' income, assets and liabilities	Surplus/deficit & assets attributable to the Takaful funds
<b>Challenges</b>	Difficult to explain financials to the shareholders	Might be perceived as Takaful operator taking over the Takaful funds

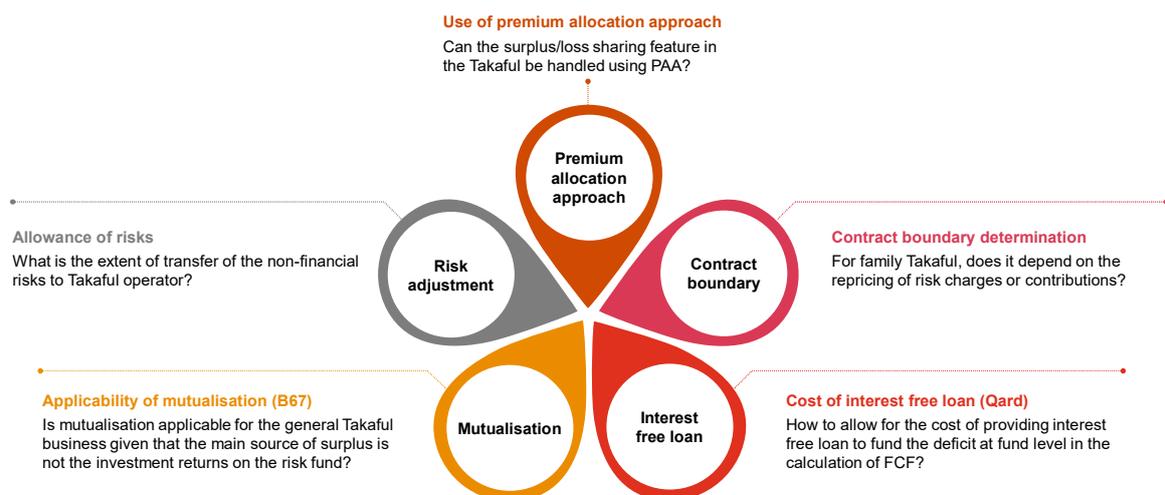
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## IFRS 17 technical issues specific to Takaful

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### IFRS 17 technical issues specific to Takaful contracts



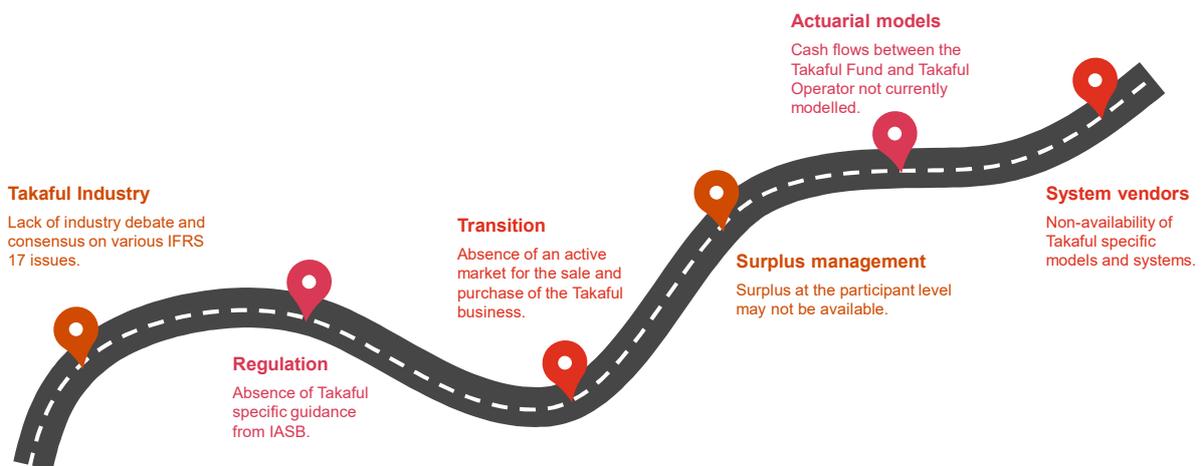
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## Significant practical implementation challenges

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### Key issues in IFRS 17 implementation on Takaful



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# Thank you

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