Benchmarking LDTI implementation

In our survey of insurance executives, we find that implementation of the LDTI standard has been complex, time-consuming, and expensive. On the plus side, they recognize that the investment to upgrade systems and processes for LDTI will lead to improved data and technology capabilities that are likely to enhance future business value.

When the Financial Accounting Standards Board issued Accounting Standards Update No. 2018-12 (ASU 2018-12) five years ago, the insurance industry knew it would require significant effort to research, design, and implement the standard. Better known as Long-Duration Targeted Improvements (LDTI), the standard is arguably the most significant change to U.S. insurance accounting in over 30 years. It revises U.S. generally accepted accounting principles (U.S. GAAP) for long-duration contracts, such as traditional and limited-payment life contracts, fixed and variable annuity contracts, disability-income contracts, and more.

LDTI became effective January 1, 2023 for SEC filers, excluding smaller reporting companies as defined by the SEC. How much effort did it take, how much did it cost, and how challenging was it? Our purpose in offering this report is to share insights from our surveys on how insurers have progressed on their LDTI journey.

We hope that this report provides the insurance industry a glimpse of the level of effort insurers expended to adopt the new standard. We also hope this report provides the 2025 adopters, i.e., SEC filers that are smaller reporting companies and all other companies adopting LDTI on January 1, 2025, helpful information for their own implementation.

The new standard, even though targeted, is certainly not simple. LDTI has substantially impacted the data, systems, controls, and processes used to measure and report insurers' financial results.

Since 2019, KPMG has surveyed individuals at insurance companies impacted by the standard, including chief financial officers, chief actuaries, accounting policy leaders, and project directors, among others, to understand how insurance companies are handling their LDTI implementation and what they consider to be the top challenges.

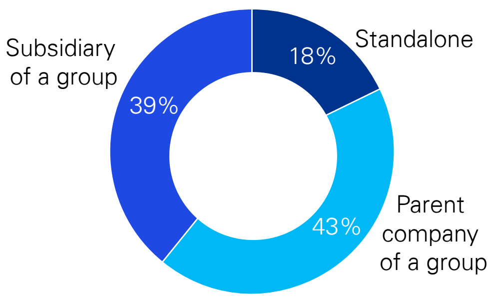
As with all our reports, we anticipate and hope that some of our conclusions will be challenged by our readers. Our intention is to provide a spark for conversations between insurance professionals and industry participants. To that end, we welcome your feedback.

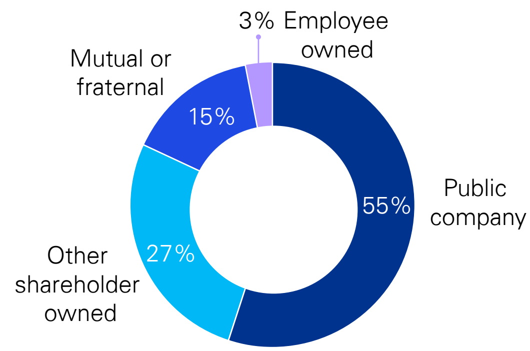
Who are the respondents?

Overall, 85 percent of survey respondents use U.S. GAAP as their primary basis for financial reporting. The remaining 15 percent use statutory accounting as their primary basis for financial reporting; however, they also use U.S. GAAP for reporting to their parent company or as a tool for decision making.

As to corporate structure, 82 percent of survey respondents are part of a group either as a parent or subsidiary. Additionally, 55 percent of the respondents are public companies.

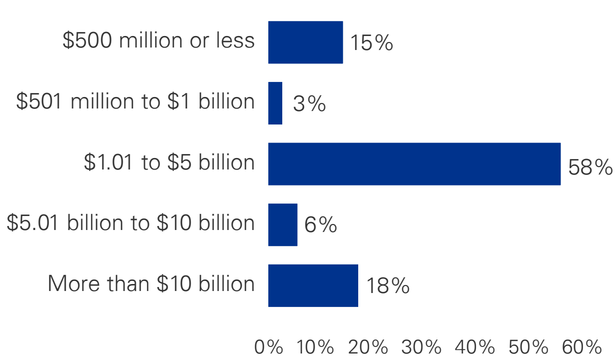
Is your company a stand-alone entity or part of a larger group of companies?



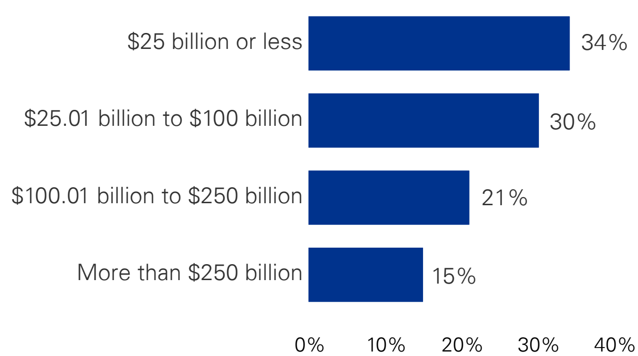


Insurance companies that responded to the survey had annual premiums ranging from $500 million or less to more than $10 billion and total assets ranging from $25 billion or less to more than $250 billion.

What are your company's annual premiums?



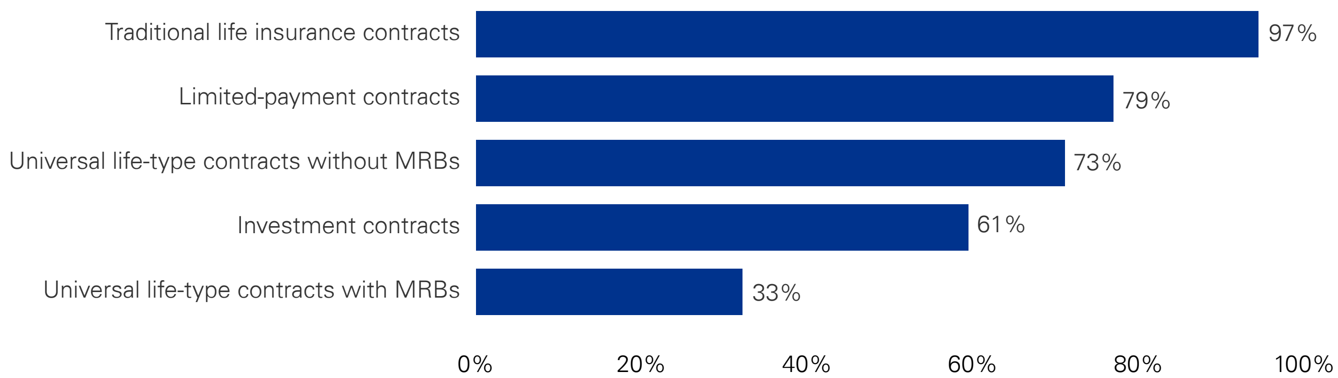
What are your company's total assets?



Direct writers comprised 94 percent of the survey respondents and the remaining 6 percent are reinsurers.

While 97 percent and 76 percent of survey respondents write life insurance contracts and annuity contracts, respectively, 45 percent write health insurance contracts and 24 percent write long-term care contracts. As to the type of contracts, the vast majority write traditional life insurance contracts, limited-payment contracts, and universal life-type contracts without market risk benefits (MRBs).

What contracts does your company write?



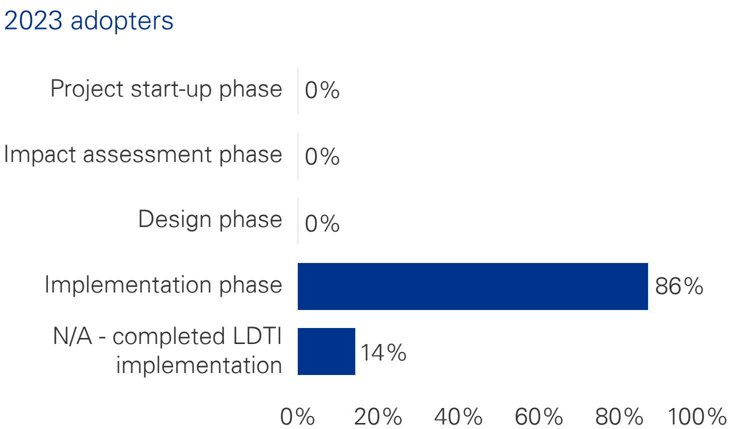
Note: Respondents were asked to select all that apply.

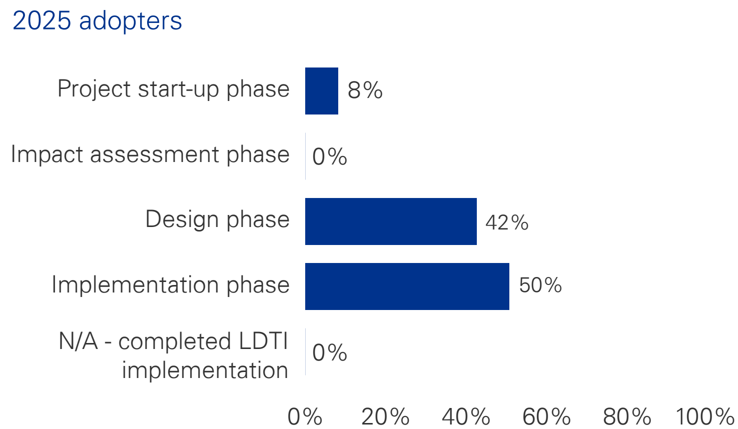
When we asked the survey respondents to identify the number of countries outside the U.S. for which they have insurance operations that were impacted by the standard, 6 percent selected 16 to 30 countries, another 6 percent selected 5 to 15 countries, and 36 percent selected fewer than 5 countries. The remaining 51 percent stated they do not have other countries with insurance operations that issue long-duration contracts.

Which project phase are you in?

Unsurprisingly, as of the survey date of March 2023, the 2023 adopters had either completed their LDTI implementation or were in the implementation phase. Conversely, the 2025 adopters were split between the design and implementation phases.

Which LDTI project phase are you currently in?





What is the cost?

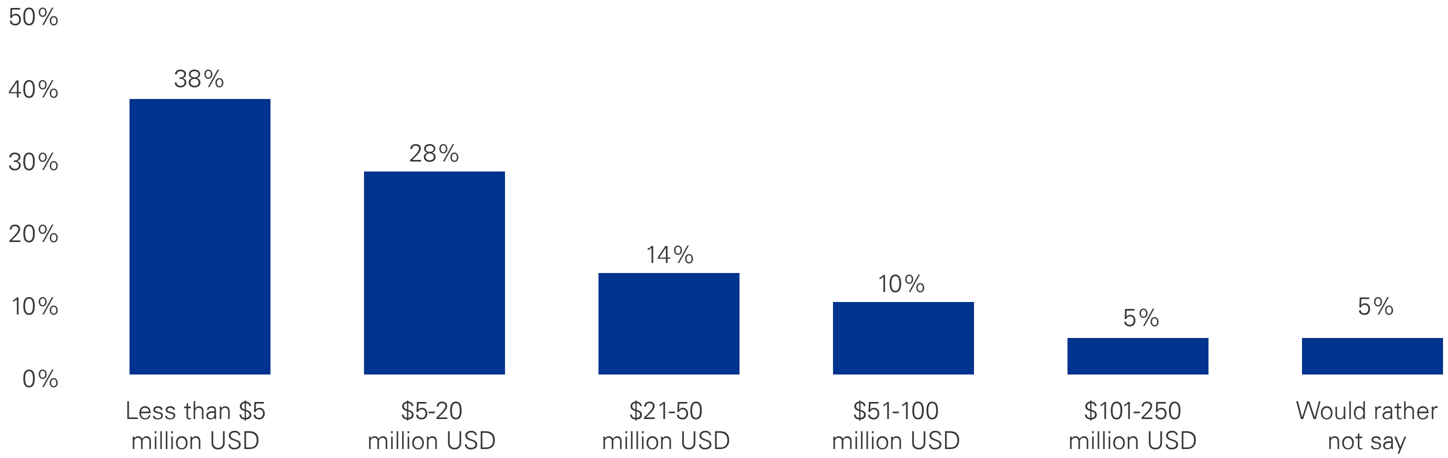
It is safe to say that the insurance industry expected the accounting change to be costly. How much did insurers plan to spend? A majority of the 2023 adopters budgeted between less than $5 million (38 percent) and $5 to $20 million (28 percent). Based on the survey results for the 2023 adopters, the average cost per company was $26.4 million, calculated pro-rata by the number of respondents for each response category.

Unlike the 2023 adopters, the 2025 adopters have a little over a year before their effective date and interestingly, have demonstrated a spending trend similar to the 2023 adopters, based on their current planned budgets. A computation of the average planned budget per company for the 2025 adopters yielded $27 million, calculated pro-rata by the number of respondents for each response category. Why are the 2025 adopters spending more? Several considerations come to mind, including:

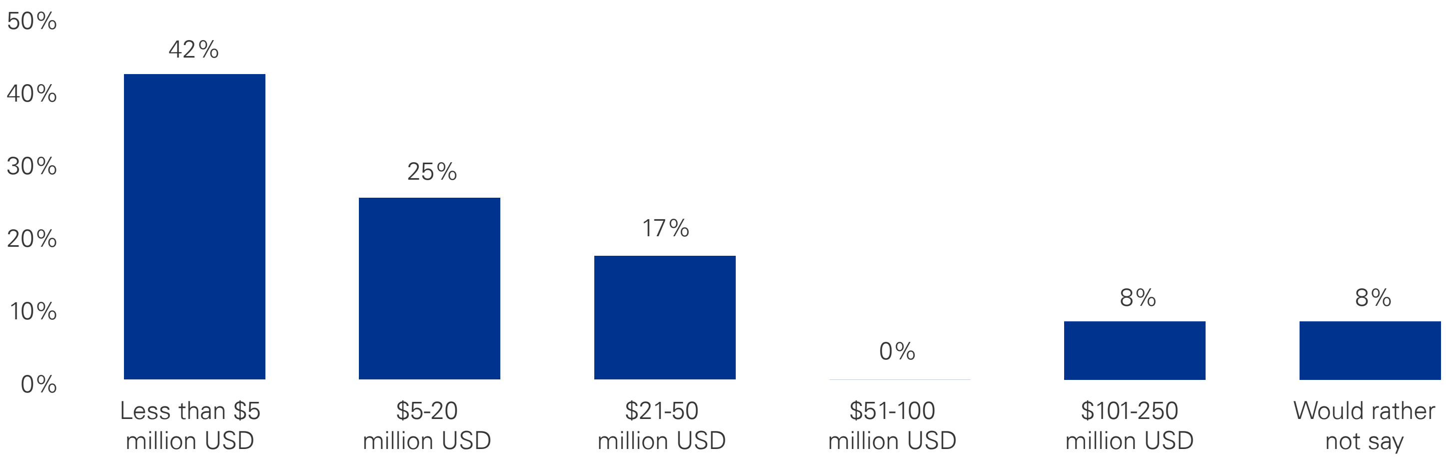
- Fewer resources within the actuarial and finance functions to take on the additional work of implementing a new standard and the need to hire external resources,
- Legacy systems are incapable of handling the new requirements under LDTI and that is spurring the need for system and process changes, and
- A less robust financial close and reporting function that requires greater enhancements to produce the required LDTI disclosures.

What is your current planned budget to implement LDTI?

2023 adopters



2025 adopters

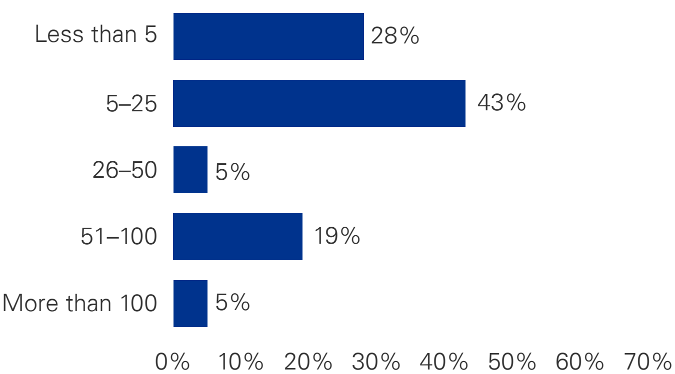


What are the resource needs?

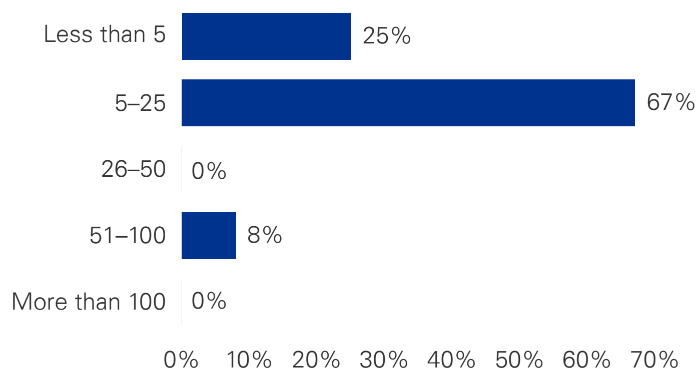
We will now explore the human capital needs for implementing LDTI. As shown below, 24 percent of the 2023 adopters had more than 51 full-time equivalents (FTEs) dedicated to the implementation project while only 8 percent of the 2025 adopters had a similar level of internal resources. This signals lower internal resource capacity for the 2025 adopters which explains the higher use of external resources; 50 percent of the 2025 adopters had significant or extensive use of external resources compared to only 28 percent for the 2023 adopters.

How many internal FTEs (i.e., employees) are currently assigned to your LDTI project?

2023 adopters

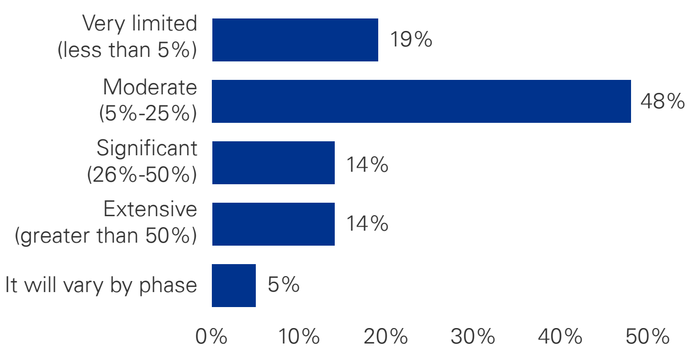


2025 adopters

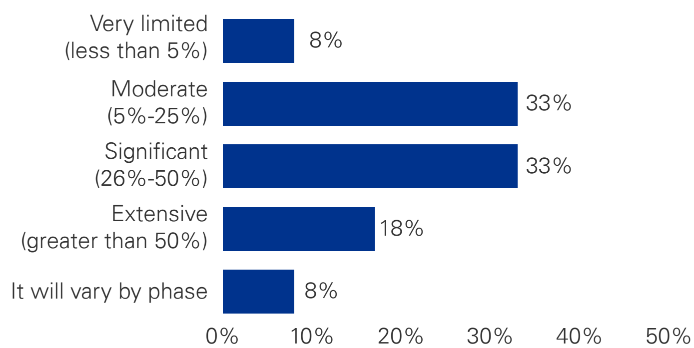


How much external assistance (i.e., contractors and consultants) have you used or plan to use to assist in implementation?

2023 adopters

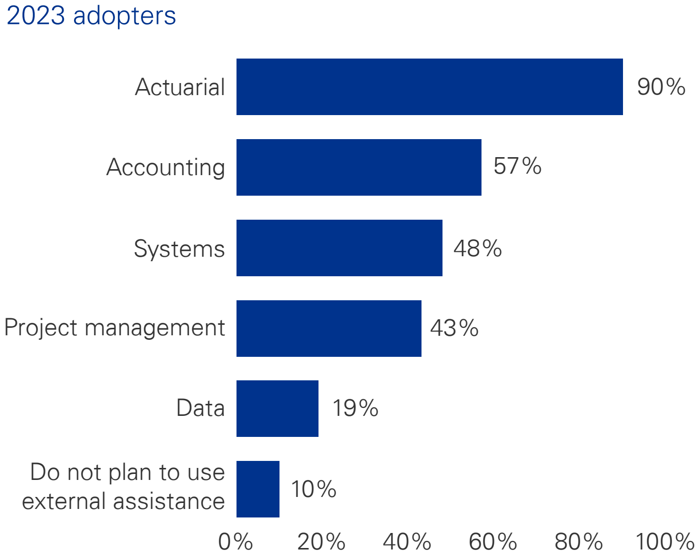


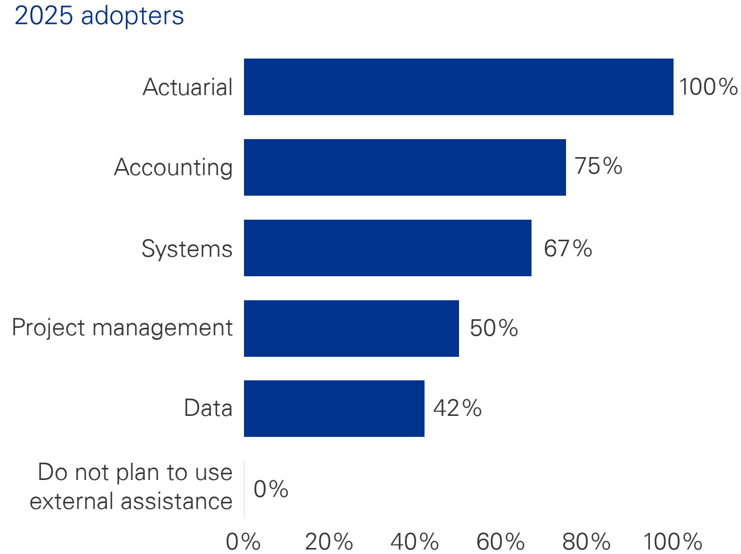
2025 adopters



In general, there is a similar trend between the 2023 adopters and 2025 adopters with respect to areas where insurers used external assistance; actuarial tops the chart followed by accounting and thirdly, systems. A deeper review of the survey results reveals a greater use of external assistance by the 2025 adopters in all areas impacted by LDTI. Lastly, we assessed the purpose of external assistance noting consistent application by both the 2023 and 2025 adopters in the top three categories, specifically as subject matter experts, to provide advisory support to the insurers whose teams remained as project leads, and to augment capacity, i.e., backfilling roles or carrying out new roles.

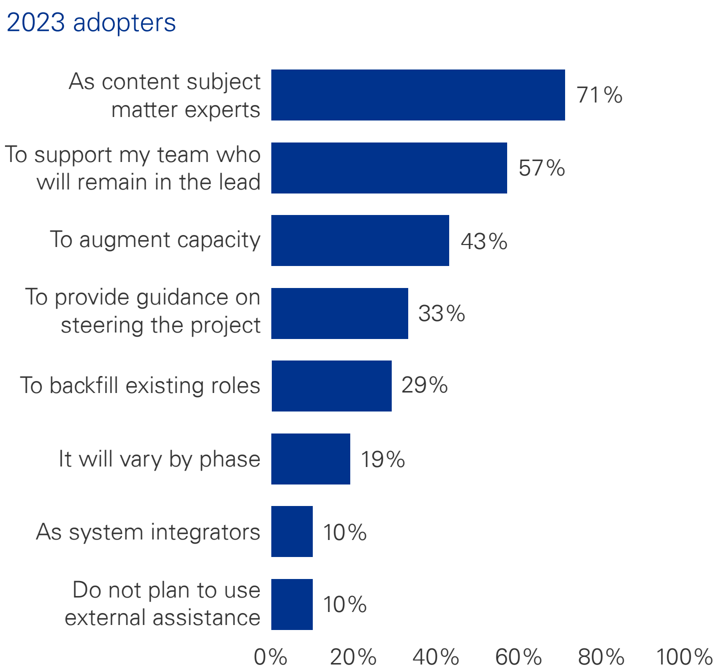
In what areas have you used or plan to use external assistance?[2]

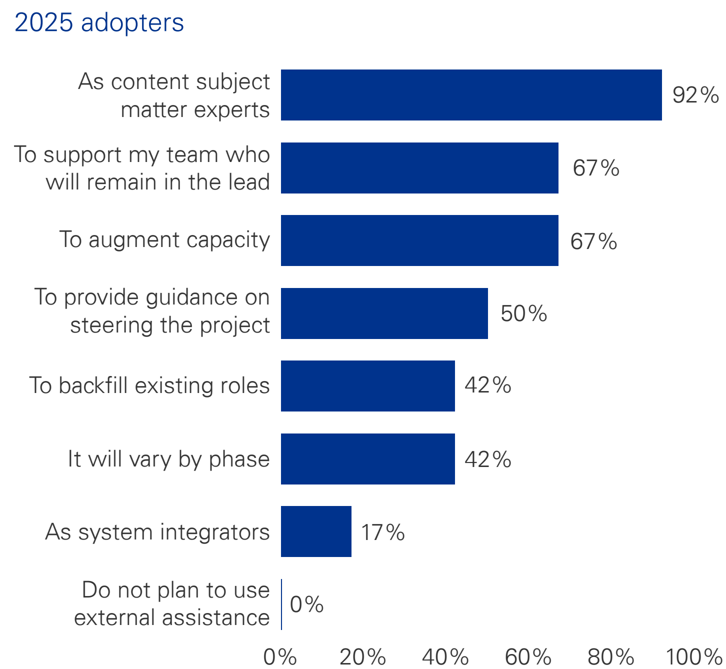




Note: Respondents were asked to select all that apply.

For what purposes have you used or plan to use external assistance such as consultants and contractors?





Note: Respondents were asked to select all that apply.

When we asked the insurers if they currently expect significant resource challenges in implementing LDTI, 50 percent of the 2025 adopters answered yes to securing sufficiently skilled people while 17 percent said yes to securing adequate funding.

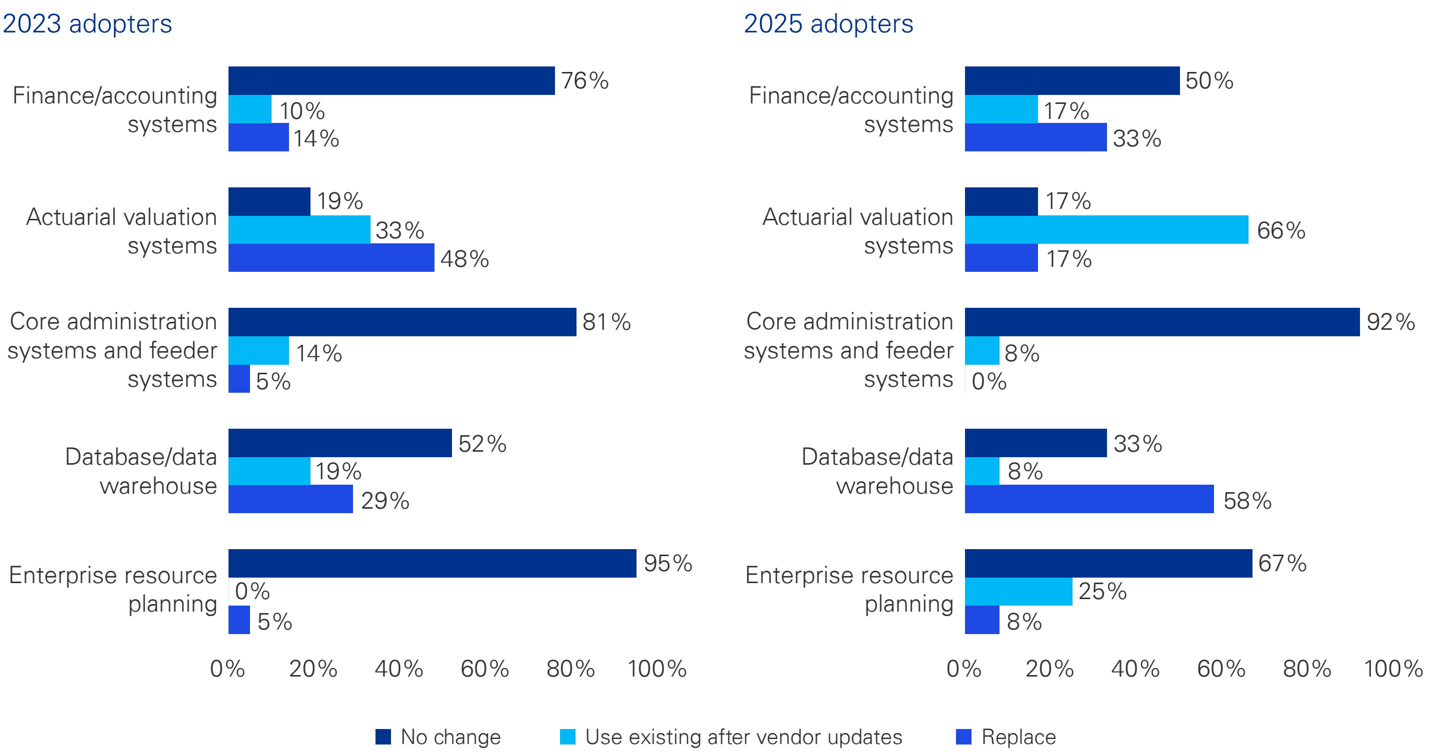
What are the technology needs?

LDTI is as much an IT and data management project as an actuarial and finance project. Implementing LDTI is undoubtedly a multi-disciplinary effort so we will now explore the technology needs.

What systems are insurance companies replacing? Overall, 40 percent of the survey respondents replaced their databases/ data warehouses while 36 percent replaced their actuarial valuation systems, and 21 percent replaced their finance/accounting systems. A comparison of the 2023 adopters to the 2025 adopters demonstrates a higher occurrence of system replacements by the 2025 adopters for databases/data warehouses and finance/accounting systems while the 2023 adopters had more actuarial valuation system replacements.

Under LDTI, contracts are being grouped into cohorts to calculate the liability for future policy benefits. LDTI also requires insurers to present disaggregated tabular roll forwards of the liability for future policy benefits and other impacted balances such as policyholder account balances, market risk benefits, separate account liabilities, and deferred acquisition costs. To facilitate roll forward disclosure preparation, certain data feeding into insurance companies' financial reporting systems is more disaggregated than what was previously required. This includes premiums, claims and reserve data. LDTI emphasizes the importance of scalable data and the need to store, control, analyze, retain, and report actuarial model output. Hence, it's no wonder that enhancements of databases/data warehouses are a priority.

What changes are you expecting for the following areas of your business?



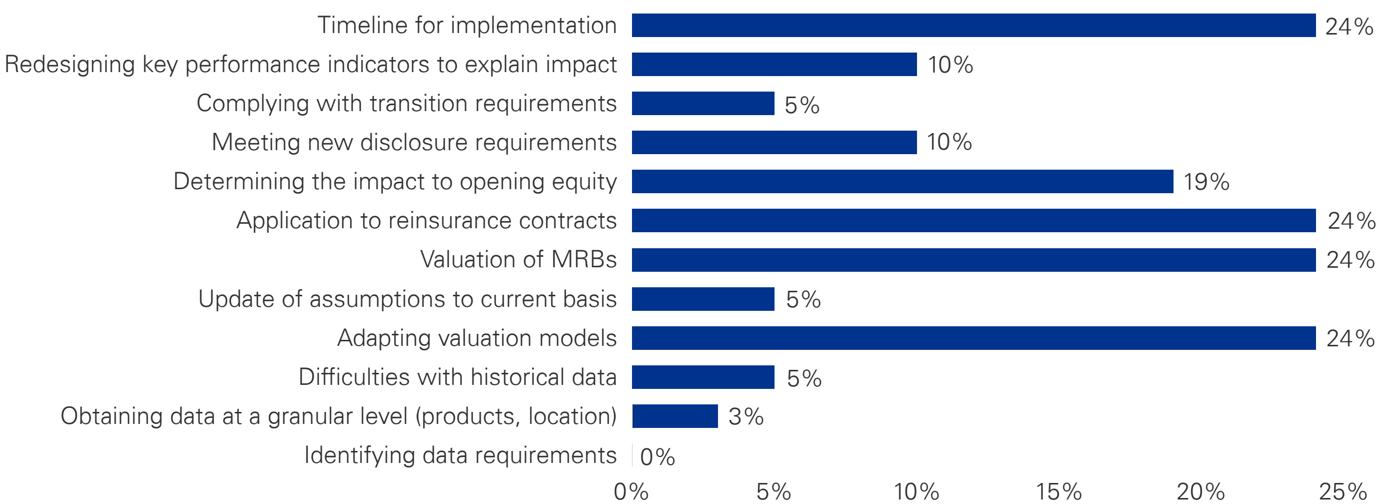
What are the top challenges?

When we asked the survey respondents to rate 16 topics of implementation, the 2023 and 2025 adopters selected 11 and 8 topics, respectively, as highly challenging. The top highly rated topics selected by the 2023 adopters were timeline for implementation, application to reinsurance contracts, valuation of MRBs, and adapting valuation models. On the other hand, the 2025 adopters chose three topics - timeline for implementation, difficulties with historical data, and obtaining data at a granular level (products, geographic location) as their top picks. It's no surprise that both groups selected timeline for implementation; companies have experienced time challenges in the implementation journey, and are continuing to do so, in the case of 2025 adopters.

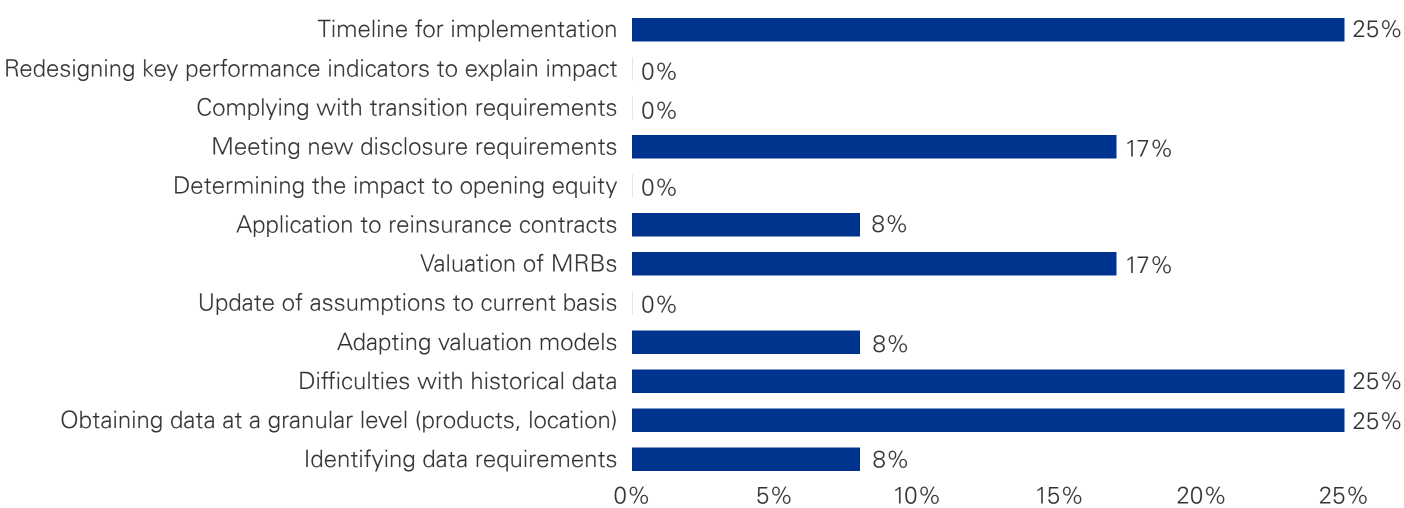
Interestingly, we have learned from our experiences that companies furthest along with their LDTI implementation projects are the ones feeling the time challenge the most. Why might that be? One needs to scratch the surface a little — the more companies do, the more they realize how hard the task is, how far-reaching the organizational impacts of the change are, and how much more work is involved than they first thought.

Rate the level of challenge with respect to your implementation of LDTI

2023 adopters



2025 adopters



Can the insurance industry declare success?

While the changes that LDTI introduces have clearly created challenges for insurers, 64 percent of survey respondents believe that the FASB's stated objectives are achieved by the LDTI changes.

Interestingly, 71 percent of the 2023 adopters support the view that the FASB's objectives are being met while only 50 percent of the 2025 adopters have the same view. Is it likely that perspectives will shift as progress is achieved and the 2025 adopters move closer to their effective date? At this time, the task ahead for the 2025 adopters may seem daunting, perhaps overwhelming. In general, respondents who did not believe the FASB's objectives are being achieved expressed concern over cost, consistency between adopters and non-adopters, and the added complexity in valuation and financial reporting.

How KPMG can help

The KPMG insurance accounting change methodology acts as a compass to help ensure that insurers ask and answer the right questions about implementation, including questions about program interdependencies and the broader business implications brought on by the change.

KPMG has a cross-functional team of subject matter experts ready to provide your company with a suite of services needed to thoroughly implement LDTI. This team consists of technical accounting, actuarial, data, finance transformation, and other insurance sector specialists with deep experience in their respective fields. Each of these areas of expertise are individually important to accounting change, but also have key interdependencies that must be considered throughout the entire implementation process.

KPMG professionals will begin their hypothesis-driven approach in a top-down rather than bottom-up gap analysis to help ensure a robust yet cost effective transition to LDTI that will result in full compliance with the accounting change. With deep market insights gained from advising leading insurers on LDTI implementation, our insurance sector specialists will leverage previous lessons learned to develop a tailored action plan. This plan will consider the complexity of each area of change, the existing gaps in actuarial and accounting processes, and will communicate the magnitude of effort required to bring your company's current state environment into compliance with LDTI.

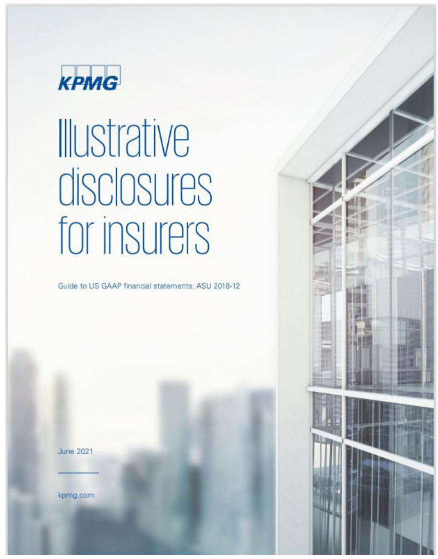
Our insurance accounting change team can bring you insights every step of the way by actively promoting knowledge transfer to your people from the outset, which will provide you with a sound base of expertise to deliver new ways of working. This value-added service will help ensure that, after the conclusion of your tailored LDTI implementation, the key stakeholders in your business will be fully equipped to maintain processes and be able to account and report in a manner that is in full compliance with regulations and provides maximum value to your investors.

Throughout the implementation, our professionals will help you understand, prepare, and address the complex challenges presented by LDTI by leveraging the KPMG tailored methodology that considers the impact of LDTI for your business in a structured way. This structure will provide insight in a manner that is tailored specifically to your business and strategic objectives.

Related thought leadership

Find these and more on the "KPMG Insurance Accounting Change Hub"

Handbook: Long-duration contracts (kpmg.us)



Illustrative disclosures for insurers adopting ASU 2018-12 (kpmg.us)

Analyst trends in LDTI

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