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LDTI Implementations: Lessons Learned

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A recent survey[1] by PricewaterhouseCoopers (PwC) revealed that meeting the new long-duration targeted improvements (LDTI) requirements—issued by the Financial Accounting Standards Board (FASB) under its US Generally Accepted Accounting Principles (GAAP)—poses significant challenges for many companies. In fact, as shown in Figure 1, 87 percent of the survey respondents considered the LDTI timeline challenging, with 61 percent saying it has been extremely challenging. This is because companies have to make significant changes, in a relatively short period of time, to systems and related processes that accumulate and transform data that insurers have not previously captured and aggregated within their actuarial models.

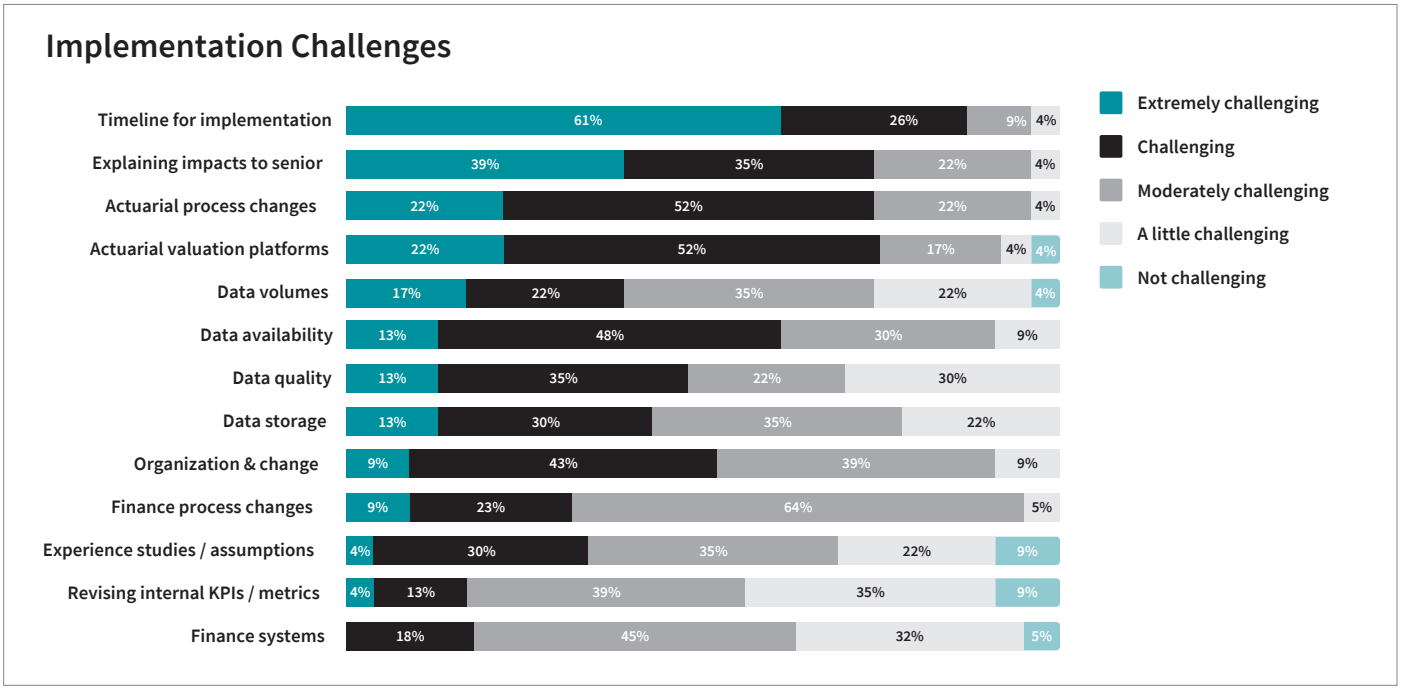
In this article, we summarize five key lessons that we have learned in implementing LDTI and share our insights on practical ways to address them. This is not an exhaustive list of implementation challenges, but companies that can successfully tackle the issues we describe should have a smoother data and systems implementation transition.

TAKING A RIGHT-TO-LEFT APPROACH

After the initial release of the LDTI standard, many insurers unsurprisingly started asking questions about data storage, processing capabilities and new software implementation. While we recognize that there is a lot to do in a short period of time, we recommend that the first step for insurers is to detail the requirements they most want to address. We frame this in the context of a "right-to-left" approach.

Simply put, a right-to-left approach starts with defining the downstream business requirements (informally referred to as the "right"). The process of cataloging those business requirements should ideally include members from the IT, accounting and actuarial functions. After defining those downstream business requirements, the insurer then works to the "left," meaning that team members diagram the upstream data and system needs. Team members continue diagramming to the left, eventually stopping at the firm's source systems (i.e., the first point in the data continuum where data are ingested or entered).

Figure 1
Results from a Recent LDTI Survey



Source: PwC. 2019. Long-Duration Target Improvement Survey. *https://www.pwc.com/us/en/cfodirect/issues/insurance-contracts/long-duration-improvement-survey-2019.html.*

By using a right-to-left approach, the three functions will be able to map out the entire data journey while maintaining focus on the end requirements throughout the process. The time the functions spend on thinking through data requirements and system changes is thus anchored in LDTI requirements.

ADOPTING AN AGILE-BASED APPROACH DURING IMPLEMENTATION

One of the common themes to keep in mind with GAAP change pronouncements is that the timeline is set, and vendor software solutions and modifications are new. Therefore you will need to do more testing than in a typical upgrade or implementation.

Using an agile-based approach with short, two- to three-week sprints for identifying and handling basic requirements and implementation scenarios early on is essential for success. Do not try to design a solution for exception cases during requirements gathering. Break down more complex scenarios into smaller pieces of work. This will help you build momentum and obtain visible results early on, providing time to explore exception cases later in the project. This will also enable a continuous delivery model and help you manage changing requirements later in the process.

Prioritizing material design items, planning the sprints of work, and working in a collaborative way with different workstreams (actuarial, accounting, IT, data and so on) is extremely important both to gain agreement and clarity on policies and to determine the underlying assumptions, parameters and principles required for successful implementation. Finally, dedicating a team of skilled technical subject matter specialists (from both business and technology functions) is critical for obtaining suitable results within tight timelines.

BEING CLEAR ON VENDOR INTERACTIONS AND TOUCH POINTS

First, strong ties with vendor teams is crucial for success. Understand that vendors are ramping up for the higher level of client support that will be required of them for this GAAP change. They also will be engaging with a number of clients at roughly the same time. Developing strong relationships early on can help enable proper support for your organization. Scheduling vendor team resources to be on-site with your team during implementation is preferable.

Second, it's important to understand in detail the key hand-off points with your vendor to facilitate proper communication of requirements for configuration. For example, does the vendor have a specific business requirement template that addresses unique areas of the product and that it expects its clients to complete in advance? Does it have a defined data mapping template so that its clients can appropriately map data elements from various sources to the vendor's target solution or module?

Third, having an upfront discussion with vendors about their release timelines for LDTI features will help your organization better plan for implementation. With new GAAP change pronouncements, it's not uncommon to have a number of releases and patches during and after go-live. Knowing the

functionalities that will be provided and the timeline will help your organization plan an appropriate rollout strategy.

When vendors upgrade and tailor their products to LDTI, it could be helpful to assess the use costs and benefits as an opportunity for larger scale, enterprise-wide platform modernization efforts.

USING ESTIMATION TECHNIQUES WHERE APPROPRIATE

Working with external auditors early in the process to agree on how to use various estimation techniques can save companies months of implementation time. However, developing a framework to determine how and where to apply approximations can be challenging.

For those blocks that are deemed immaterial, one estimation worth considering is to leave current GAAP as it is. The rationale behind this is that the block is so immaterial that its impact on the overall balance is minuscule. This approximation is ideal for those companies that report under a consolidated balance sheet.

We also see companies assessing the appropriateness of approximation techniques based on potential impact (high, medium, low) and operational challenges (hard, moderate, easy). For example, updating discount rates may not be difficult, and because the potential impact is high, it probably makes sense to update them. On the other hand, combining material and nonmaterial cohorts could be operationally onerous and have a minimal impact. Companies can perform this analysis at the block level for each of the key changes that LDTI implementations require.

TAKING A PROACTIVE APPROACH TO MODEL TESTING

As described in PwC's recent paper on LDTI model validation[2], taking a proactive approach to testing is critical for success. Waiting to compile and document all existing test plans can potentially delay the project timeline and result in retesting if issues are not discovered early. Breaking down test plans into manageable pieces and testing more frequently (e.g., at the end of each sprint) will make the process more efficient. This method works as long as the larger testing project plan is periodically reviewed and the test case inventory is continuously updated for completeness. When building test plans, consider these three areas:

- **Data:** If test data are not available, use sample data (create your own) and start performing unit testing. This can help you catch errors in models early in the process. Using sample data is an established practice, as it helps test paths that may be encountered rarely or not at all with real-life data.
- **Models:** All the models need not be completely coded to start testing. Models can be tested piecemeal. For instance, if the premium piece of the model is coded first, it can be tested initially and then integrated with the benefits piece after that part is completed.
- **Reports:** Once again, if the data are not available for testing, run the reports anyway and use sample or test data to ensure reports are generated appropriately for the test case being considered.

We recognize that there are many challenges with LDTI implementation, but by taking these five key steps, you should be better positioned for a successful and sustainable transformation. ■

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ENDNOTES

1 PwC. 2019. Long-Duration Target Improvement Survey. *https://www.pwc.com/us/en/cfodirect/issues/insurance-contracts/long-duration-improvement-survey-2019.html.*

2 PwC. 2019. A Better Approach to LDTI Model Validation. *https://www.pwc.com/us/en/cfodirect/issues/insurance-contracts/ldti-model-validation.html.*