

Mr Hans Hoogervorst
Chairman
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

2 February 2017

Dear Mr Hoogervorst,

IFRS17 – completion of Insurance Contracts Standard

I am writing as a follow up to the meeting of Gerald Harlin, Dieter Wemmer and I with you and fellow IASB members on 11 January and, as set out later in this letter, share some editorial suggestions for the final drafting of the standard.

It was helpful to discuss our different perspectives on project completion to achieve a high quality standard. We acknowledge that you will not be sharing the fatal flaw draft with the Forum or undertaking a further period of assessment prior to issuing the standard. We also note that you consider that further deliberations by the IASB or with the industry on technical aspects of the standard are unnecessary.

However, as we discussed in our meeting, there are areas in which, in our view, further change is necessary. These include, but are not limited to:

- level of aggregation (for example for the unnecessary complexity of the requirement to separate contracts that have no significant risk of becoming onerous from other profitable contracts);
- accounting mismatches due to, for example, the IASB approach to risk mitigation (hedging and reinsurance) and the mandated use of a locked-in discount rate for contracts that are not accounted for under the variable fee approach (VFA), and.
- the approach to release of the Contractual Service Margin (CSM) to the income statement.

Notwithstanding these broader topics, we appreciate your willingness to accept comments of an editorial nature that might assist with the drafting of the final standard. Our editorial comments are as follows:

Level of Aggregation

As regards extracts from fatal flaw draft that were published on the IASB website on 10 January we note the following points:

Paragraph 14:

We do not believe it is appropriate to include references to specific product types (e.g. annuities, whole-life, term-life). Such examples may result in contracts with similar risks inappropriately being separated into different portfolios. For example, long-term term-life business may actually have very similar risks to whole life

business. The standard should be principles based with the guidance preventing too narrow an interpretation.

Paragraph 16:

We understand that the IASB's intention is to allow an approach that is closer to "top-down" for the onerous contracts test than hitherto contemplated by the IASB. However, there is significant uncertainty as to whether paragraph 16(b) achieves this objective. While permitting the use of reasonable and supportable information (which could, for example, include pricing information) to carry out the assessment suggests a top-down approach, the requirement that a set of contracts will either "all be onerous" or "will contain no onerous contracts" suggests that contract level (bottom-up) calculations are required. Furthermore, it is not clear how to interpret the term "set of contracts".

Paragraph 19: Requirement for groups of contracts to be issued "no more than one year apart"

At our meeting we questioned the relevance of the new requirement that the reporting entity should not group contracts that are more than one year apart. This will lead to operational complexity with no apparent benefit to users and we would prefer that the requirement is removed. We understand that the motive for the new requirement is to ensure that the CSM runs off over the contract duration. However, we note that paragraphs 67 and B107 of the July 2016 testing draft already include general provisions regarding de-recognition and release of CSM over coverage periods. In our opinion the new grouping restriction is not helpful and we request that the final version of the standard provide relief from this unduly burdensome requirement.

We also discussed how the "no more than one year apart" grouping requirement worked alongside the IASB recognition that the assessment of onerous contracts should take account of situations where there is a mutualisation of benefits to policyholders across contracts, including on an intergenerational basis, with an open portfolio approach. Our understanding from the discussion is that the mutualisation feature should be viewed as the overarching principle so as to enable the "no more than one year apart" requirement for such contracts to be rendered not relevant in such circumstances. However, it is not clear how this will be written into the standard and we request that the drafting is sufficiently transparent to facilitate the intention to be enabled with confidence by preparers.

Changes in estimate – experience variances

The July 2016 draft required that all experience adjustments impacting future cash flows arising from non-financial risk (such as mortality and persistency) and not affecting underlying items should be taken to the CSM. This approach was then changed by the decisions at the November IASB meeting so that the impact is required to be taken to P&L. The variances comprise two components namely the variances on current and future period cash flows. It would be more appropriate, where operationally feasible and economically relevant, for the variances related to future period cash flows to be taken to the CSM.

Scope of the variable fee approach

The Forum has previously made the case that cliff edge effects can arise from the scope of the VFA. In particular, concern has been raised that different results may arise for contracts where the contractual terms are insufficiently binding to meet the IFRS 17 criteria.

We acknowledge the IASB's view that in some scenarios policyholder benefits for such contracts may be different from when the benefits are contractual. This may be relevant to determining capital requirements but it is not clear that it should drive a systemically different approach to measurement and the related performance reporting.

We remain of the view that customary business practices and obligations are important features that can be equivalent to a contractual requirement in all but extreme scenarios. Therefore, we welcome the IASB staff's view as expressed in the November agenda papers that contracts can be written, oral or implied by an entity's customary business practices. We would urge that this is reflected in the final drafting of the standard.

Scope of the premium allocation approach (PAA)

The PAA has long been expected to be able to be applied by non-life insurers for the majority of their business. However, some of our members have heard informally that the final drafting of the standard may include changes to reduce the scope of when the PAA can be applied, in particular for contracts with investment components. We urge the IASB not to make late changes that would significantly reduce the scope criteria in the final standard.

Hedging

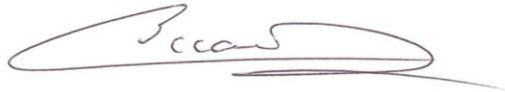
We appreciate that at its November meeting the IASB decided to widen the scope of the hedge adjustment to include changes in the variable fee under the VFA. Notwithstanding that the adjustment is prospective only this is a welcome development.

We discussed at our meeting our view that a hedge accounting solution should apply across all types of business and acknowledge that insurers typically manage their exposures on a macro basis for different types of financial risk. We acknowledge your view that this will not be possible before the standard is issued. However, as we explained, it is inevitable that this will lead to explanation of performance reporting being complicated with accounting mismatch effects needing to be disentangled from the total results to establish underlying performance by the publication of an alternative performance measure.

Finally, whilst we acknowledge that you do not wish to share the fatal flaw draft with the Forum, we stand ready to assist you on the finalisation of the standard.

We remain committed to support the IASB as it seeks to finalise the standard.

Yours sincerely

A handwritten signature in dark ink, appearing to read 'Nicandrou', with a large, sweeping underline that extends to the right.

Nic Nicandrou
Chairman

Copy:
Gérald Harlin, Chief Financial Officer, Axa Group
Dieter Wemmer, Chief Financial Officer, Allianz SE
All other CFO Forum members
Olav Jones, Deputy Director General, Insurance Europe