Roger Marshall
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European Financial Reporting Advisory Group
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Belgium

19 November 2015

Comments on Draft letter from EFRAG to the European Commission

Dear Mr Marshall:

This letter is from the European Insurance CFO Forum ("CFO Forum"), a body representing the views of 21 of Europe's largest insurance companies and Insurance Europe, which is the European (re)insurance federation whose members are the national insurance associations in 34 countries, representing 95% of the premium income of the European insurance market.

We are very appreciative of EFRAG's efforts to date and for EFRAG's understanding of the insurance industry's significant concerns regarding the impact from the misalignment between the effective dates of IFRS 9 and IFRS 4 Phase II. We continue to support EFRAG's view that "all business other than those carrying out insurance activities are required to account for their financial instruments in compliance with IFRS 9 in 2018 and business carrying out insurance activities are permitted to do so".

We would be grateful if the letter to be sent by EFRAG to the European Commission could be augmented for our key concerns with regards to the improvements needed for the preferred Deferral Approach to be workable, the inappropriateness of the Overlay Approach, and how cost considerations should be assessed.

The Deferral Approach

We strongly support the Deferral Approach, provided that its scope is defined adequately. In this respect, we support the principle of predominance for the scope of the Deferral Approach. We believe that predominance should be determined based on qualitative principles reflecting a range of factors (which could include but should not be limited to whether an entity is a regulated insurance entity) so that the principles would permit all relevant insurance entities to be able to apply the Deferral Approach. Utilising a principles-based predominance criterion would be consistent with the principles-based nature of IFRS and would accommodate the different balance sheets of insurers around the globe.

We agree that illustrative examples with quantitative assessments could be included as guidance to support an overall assessment of the predominance principle. However, predominance cannot be simplistically defined using only a rigid quantitative test of "IFRS 4 insurance liabilities as a percentage of total liabilities". Using only a formula to make this assessment will lead to unintended consequences of excluding potentially many relevant insurance entities from the scope of the Deferral Approach.

Furthermore, a test based on IFRS 4 insurance liabilities as a percentage of total liabilities would exclude several liability balances that may be clearly related to insurance activities, such as derivative liabilities (which hedge insurance activities), non-controlling interest in consolidated investment funds (which are classified under IFRS as liabilities), funding liabilities and investment contracts carried at fair value through profit and loss and other insurance related liabilities (for example payables arising from insurance/reinsurance operations and policyholder payables). Any examples used to illustrate the predominance principle should adequately reflect these liability components. We

refer to our earlier document provided to the EFRAG Board that illustrates the significance of this issue and the impact on the share of members of the CFO Forum that would qualify for deferral. As requested by the EFRAG staff, we are currently providing additional supporting detailed information.

We support the IASB's proposed application of a predominance assessment at the reporting entity level for insurance groups. However, a solution is needed to ensure that insurers that are part of a conglomerate (e.g. bancassurers) are also able to elect to defer IFRS 9 until IFRS 4 Phase II is implemented. We believe that comparing "insurer to insurer" is more important and meaningful than comparing insurance activities with non-insurance (e.g. banking) activities within a conglomerate. Without this comparability, those insurers who are not able to utilise the Deferral Approach will face adverse consequences. As such, whether an insurer operates standalone or is part of a conglomerate should not impact the ability to apply the Deferral Approach. Applying the Deferral Approach at the level of the insurance operations within the conglomerate (i.e. lower than reporting entity level in the specific case of conglomerates) with permitted roll-up into group reporting will help to address this conglomerate issue. We would be pleased to continue to work with EFRAG on a solution that addresses the need of both insurance groups and conglomerates.

The Overlay Approach

The Overlay Approach does not address our key concerns and, as a result, is not the preferred approach for our members.

There are a number of concerns with the Overlay Approach which would make it very difficult and costly to apply in practice:

- It requires an insurer to run multiple IT processes in parallel (IAS 39 and IFRS 9).
- It requires tracking of the numbers as both data streams need to be fully aligned. This tracking will be very complex and may create audit implications that should not be underestimated from a cost perspective.
- Resource constraints may apply and additional people may need to be recruited only for a short period of time.
- There is no existing software that can accommodate this situation.

A primary driver for insurers is to provide meaningful and understandable financial information to the users of our financial statements. The Overlay Approach will result in multiple significant changes in a short period and, therefore, will be confusing to users. Furthermore, the Overlay Approach does not eliminate the effects of accounting mismatches in equity. For example, a bond backing an insurance liability which is currently recognised at amortised cost under IAS 39 may have to be recognised under IFRS 9 at fair value through the profit or loss. Applying the Overlay Approach to transfer that fair value movement from the income statement to equity would still result in volatility in equity.

Cost Considerations

Our primary concern is to produce meaningful financial statements. Costs are a secondary issue but one that cannot be ignored. It is very costly to implement IFRS 9, especially when the implementation must be done twice. Furthermore, this cost is not accompanied with any significant benefits. Without the Deferral Approach, insurers would have to incur the cost of IFRS 9 in 2018 and then again when IFRS 4 Phase II is implemented. This cost concern remains if the Overlay Approach is utilised; in fact, as we note above, the Overlay Approach would be even more costly as insurers would face the cost of implementing IFRS 9 as well as developing the temporary systems and processes to track the Overlay Approach adjustments while incurring the cost and operational difficulties of still having to concurrently maintain their existing IAS 39 systems (for example to track impairments on an IAS 39 basis).

For all the reasons noted above, we conclude that the Deferral Approach is the most realistic and operationally feasible approach and will be the most pragmatic solution, which will avoid providing confusing information to users. During the history of the development of IFRS 4 Phase II and IFRS 9 the European insurance industry has consistently requested for an alignment of their effective dates.

Summary

We agree with EFRAG's assessment that there is uncertainty as to whether the IASB will provide an appropriate IFRS 9 deferral remedy when it makes its final decisions. As such, we strongly believe that the endorsement of IFRS 9 for insurers must not be considered until the IASB has finalised an appropriate deferral solution for all relevant insurers.

We appreciate EFRAG's efforts and its continued support on this matter. We look forward to continuing to work with EFRAG to resolve this important matter.

Yours sincerely,

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