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IFRS Phase II and Solvency II: The Current Challenges

Tim Harris


IFRS II Solvency II – A unique opportunity



- Solvency II and IFRS Phase II both under development– a unique opportunity
- Key Challenges
 - Establishing a coherent framework for IFRS Phase II and Solvency II
 - Aligning of timetables
 - Ensuring consistent measurement of insurance liabilities
 - Effective and efficient implementation
- European regulators move to an economic basis for solvency reporting is a major step forward.
- We advocate an economic approach for both IFRS Phase II and Solvency II

A unique opportunity to bring solvency and financial reporting onto a coherent basis

Establishing a coherent framework for IFRS II and Solvency II



Challenges
Timing
Key Issues
Conclusion


The Solvency II Framework directive advocates compatibility / consistency with IFRS

“Valuation standards for supervisory purposes should be compatible with international accounting developments” (paragraph 27)

“The calculation of technical provisions should be consistent with the valuation of assets and other liabilities, market consistent and in line with international developments in accounting and supervision” (paragraph 31)

We need a coherent framework and consistent measurement on an economic basis

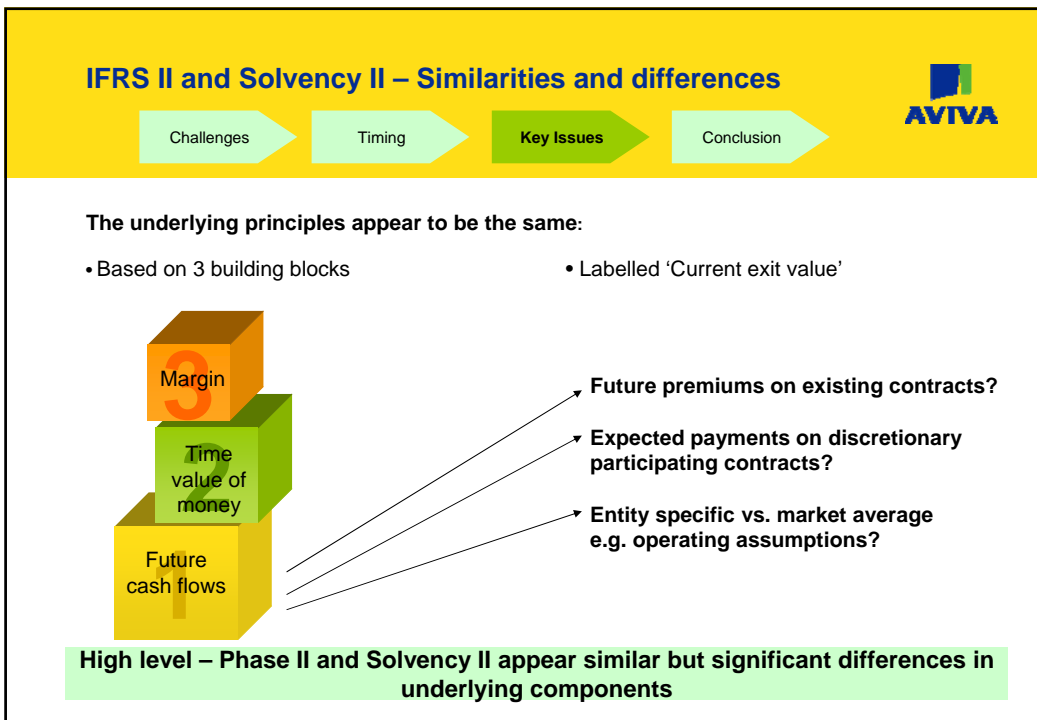
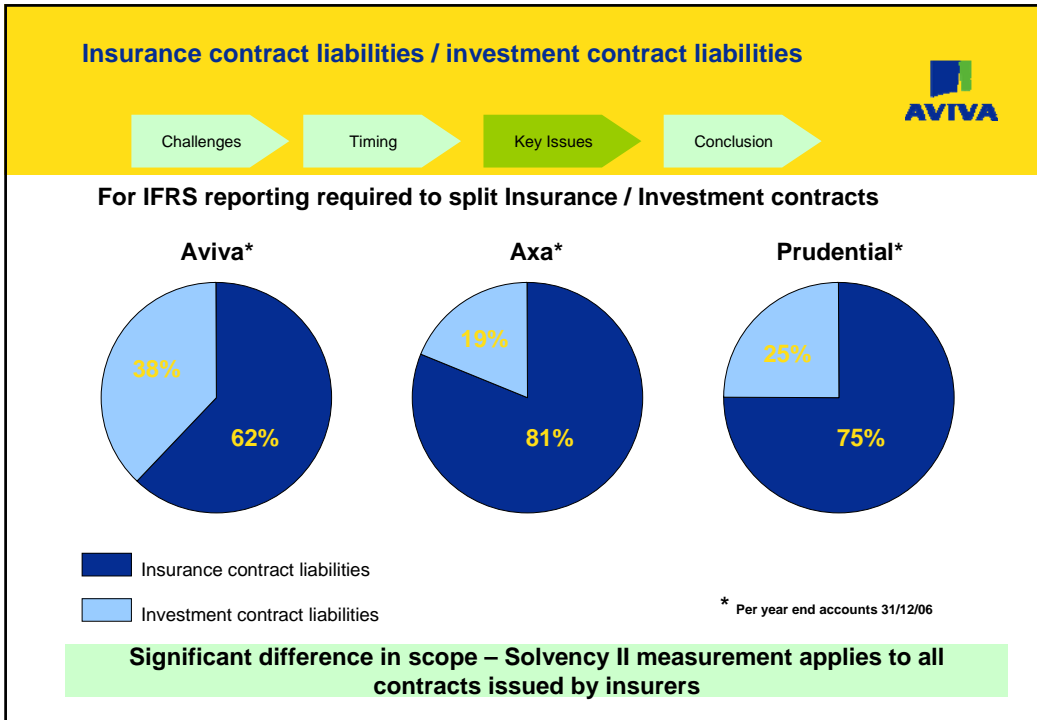
Current timeline




Challenges
Timing
Key Issues
Conclusion

2007	2008	2009	2010	2011	2012
IFRS Phase II					
Discussion Paper	Exposure Draft		IFRS		Effective?
↑ May 2007	↑ 1 st half 2009		↑ 2010 or 2011?		
Solvency II					
Framework Directive		Level 1 Dir	Level 2	Level 3	Effective
↑ 10 July 2007	↑ 1 st half 2009	↑ Oct 2009	↑ 2 nd half 2010	↑ Autumn 2012	

Timetable remains uncertain - solvency II likely to overtake phase II



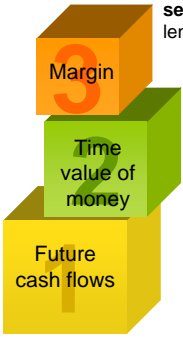
“Current Exit Value” – Does IFRS Phase II and Solvency II really mean the same thing?



Challenges
Timing
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IFRS Phase II - “the amount an insurer would expect to pay at the reporting date to **transfer** its remaining contractual obligations immediately to another entity” (Discussion paper paragraph 93)


Solvency II Framework Directive - “liabilities shall be valued at the amount for which they could be **transferred or settled**, between knowledgeable willing parties in an arm’s length transaction.” (Article 73)



- Purpose of risk margin
- Risk margin calibration
- Service margin


Differences between IFRS Phase II and Solvency II measurement bases may have been under-estimated

Practical and Implementation Considerations




Challenges
Timing
Key Issues
Conclusion

- The time and cost of implementing the proposals should not be underestimated
- We must remember the “do-ability” test
- Financial and Regulatory reporting bases both subject to fundamental and uncertain change
- The new bases should encourage and not detract from economic capital and risk management developments



Both developments must be practical to implement

Conclusion



Challenges → Timing → Key Issues → Conclusion

- Both IFRS Phase II and Solvency II should be aligned to the economics that drive our business.
- They should take into account the advances in economic capital management and incentivise good risk management practice.
- We need a coherent framework for:
 - internal management
 - financial reporting
 - regulatory reporting
- To make the implementation effective and efficient the timetable should be aligned as far as possible.
- We must maintain momentum on both projects.