

22 November 2019

Ms Heidi Richards
General Manager, Policy Development
Policy and Advice Division
Australian Prudential Regulation Authority
Level 12, 1 Martin Place
SYDNEY NSW 2000

By email: insurance.policy@apra.gov.au

Dear Ms Richards

Integrating AASB 17 into the Capital and Reporting Frameworks for Insurers

The Insurance Council of Australia¹ (Insurance Council) appreciates the opportunity to comment on APRA's Directions for Integration of *AASB 17 Insurance Contracts* into the Capital and Reporting Framework for Insurers. We would also like to thank APRA for meeting with our members, including on 14 November 2019 at the AASB TRG forum.

The Insurance Council and its members note that:

“There remains uncertainty regarding the final form of the accounting standard. APRA is monitoring the International Accounting Standards Board (IASB) process, and the outcome may impact APRA's view on integration of AASB 17 into the reporting and capital framework.”²

Given the uncertainty, we welcome APRA's communications on the topic, and encourage APRA to continue to provide guidance on its prudential treatment and reporting requirements in a timely manner. This will assist insurers in managing the risks associated with the transition to *AASB 17*.

¹ The Insurance Council of Australia is the representative body of the general insurance industry in Australia. Our members represent approximately 95 percent of total premium income written by private sector general insurers. Insurance Council members, both insurers and reinsurers, are a significant part of the financial services system. June 2019 Australian Prudential Regulation Authority statistics show that the general insurance industry generates gross written premium of \$48.4 billion per annum and has total assets of \$128.4 billion. The industry employs approximately 60,000 people and on average pays out about \$151.4 million in claims each working day.

Insurance Council members provide insurance products ranging from those usually purchased by individuals (such as home and contents insurance, travel insurance, motor vehicle insurance) to those purchased by small businesses and larger organisations (such as lenders' mortgage insurance, product and public liability insurance, professional indemnity insurance, commercial property, and directors and officers insurance).

² p1 APRA Letter *Information Request and Consultation on Directions for Integration of AASB 17 Insurance Contracts into the Capital and Reporting Framework for Insurers* (27 September 2019)

Granularity for regulatory reporting

One area in which greater clarity would be particularly welcomed relates to APRA's proposed increase in the granularity of its reporting groups. This potentially represents a significant piece of work additional to *AASB 17* implementation, although we note APRA's comment at the 14 November 2019 AASB TRG meeting that APRA is not intending to materially increase the number of product groupings but instead to target specific high risk products. We also understand from that meeting that APRA will provide details of its proposed increase in granularity in a discussion paper to be released in 2020. The sooner APRA can disclose those details, the easier it will be for insurers to integrate this into their *AASB 17* implementation programs.

In addition, APRA is proposing that, for prudential reporting, groupings used to distinguish onerous contracts under *AASB 17* must not extend across APRA reporting groups. The Insurance Council's members query how this operates in relation to contracts that cover multiple classes of business given that *AASB 17* sets the insurance contract as the lowest level of granularity.

One interpretation of APRA's indicative approach is that insurers would be required to conduct onerous contract testing at APRA's class of business level rather than at the portfolio levels determined by the insurer in accordance with their interpretation and application of the standard. In line with discussions with APRA at the AASB TRG we understand this may not be APRA's intention. Therefore, we would appreciate early clarification as to whether APRA intends to require determination of onerous contracts at the APRA class of business level and how the conflict with *AASB 17* can be addressed.

Our preference is that insurers determine portfolios for the purpose of applying *AASB 17* and identify onerous contracts in accordance with the requirements of *AASB 17* and then attribute any loss component appropriately across APRA classes of business for reporting purposes.

We believe any request for more granular reporting should be restricted to reporting and not to informing accounting standard interpretation, accounting policy selection and valuation methodology and mandating that portfolios be set no higher than the APRA class of business level would cause significant dual reporting burden, as we would be required to run permanent dual modelling and accounting which would be excessively costly on an ongoing basis.

Timing for integration into APRA's prudential frameworks

The Insurance Council's members are concerned about the proposed 1 July 2023 commencement date given the costs associated with maintaining dual accounting systems during the transition period. To mitigate these costs, we would encourage APRA to explore alternatives that could accelerate the timing for integration to align it with *AASB 17* adoption. This could include the incorporation of trial reporting on an *AASB 17* basis ahead of the effective date to provide APRA with sufficient comparative data to bring forward the commencement date.

In addition to APRA's broad timeframe, we would appreciate clarity on:

- When will APRA request a full impact assessment and to which entities will this apply?

- If dual reporting is required for a period after the mandatory application date of *AASB 17* on 1 January 2022, will APRA limit the dual reporting under the superseded accounting standard to APRA returns/forms only? Or will this apply to other APRA deliverables such as the Insurance Liability Valuation Report (ILVR)?
- If dual reporting is required, is it possible to request an extension to reporting deadlines for the dual reporting period due to the Transition Reconciliation template from *AASB 1023* to *AASB 17*?
- What consideration has APRA given to the IAIS ICS updated requirements which are also field testing the impact of IFRS 17? Will these be integrated?

Specific directions contained in APRA's Appendices A and B

Approaches for measuring insurance contract assets and liabilities [Appendix A(a)]

We support APRA's approach.

Contract boundary determination [Appendix A(b) and B(a)]

The Insurance Council recognises that APRA is awaiting the outcome of the IASB's deliberations on the timing for recognising an underlying insurance contract and related reinsurance arrangements. Any requirement to produce reporting for APRA using the legal contract duration instead of the contract boundary principle in *AASB 17* will necessitate the production of two separate sets of accounting statements, particularly for insurers with long-dated reinsurance contracts.

As such we recommend that APRA adopts the *AASB 17* contract boundary requirements for all APRA reporting and simply makes adjustments for capital measurement to reflect any obligations not captured in the contract boundary. We note this is more likely to occur when the contract boundary is shorter than the legal contract duration. We also note that currently many reinsurance contracts cover underlying contracts which have significantly different contract periods and therefore we do not see this as something APRA would need to adjust APRA reporting for under *AASB 17*.

Discount rate [Appendix A(d) and B(c)]

A number of the Insurance Council's members support the approach outlined by APRA in its letter. In addition, for regulatory capital purposes, we would encourage APRA to mandate a range of illiquidity premiums and allow insurers to potentially choose from within that range.

Calibration of capital charges [Appendix B(b)]

We would welcome clarity on the timing of APRA's announced QIS, and on whether this would lead to higher capital requirements.

Acquisition costs [Appendix B(d)]

We support APRA's approach.

Reinsurance default risk [Appendix B(e)]

We are concerned about the possible double counting of default risk in situations where reinsurance is undertaken with a non-APRA regulated reinsurer.

Risk adjustment and APRA risk margin [Appendix B(j)]

We would welcome additional clarity regarding the intent underlying the proposals.

Other considerations

The Insurance Council notes that APRA is currently consulting on the implementation of its New Data Collection Solution. At a recent workshop held on that topic, APRA noted that the implementation of *AASB 17* will impact 70 to 80 per cent of the forms for insurers. Given the significant systems changes required of insurers to adopt the New Data Collection Solution and to implement *AASB 17*, we would encourage APRA to coordinate both programs so as to mitigate the cost of implementation.

If you have any questions or comments in relation to our feedback, please contact John Anning, the Insurance Council's General Manager Policy, Regulation Directorate, on (02) 9253 5121 or janning@insurancecouncil.com.au.

Yours sincerely



Robert Whelan
Executive Director and CEO