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***Insurance Breakout
Session***
Paraic Joyce

Agenda

- Accounting update
 - IFRS for insurance contracts
 - ASB and IFRS conversion
- Solvency II update
- Other regulatory/governance matters
- Insurance Banana Skins 2011



Accounting update

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IFRS for Insurance Contracts

Why the need for a new standard?

***Insurance
accounting
TODAY is a
black box***

- Accounting for insurance contracts TODAY
- IFRS 4 (Phase I) is a temporary solution:
 - Wide variety of
 - accounting practices for different contract types and jurisdictions
 - measurement models
 - Lack of comparability and transparency
 - Current insurance accounting does not give users relevant information

IFRS for Insurance Contracts

Views on current today's accounting for insurance

“More information is better than less, I guess.”

“It's very difficult to gain a clear economic view of where profitability comes from.”

“Non-GAAP numbers always seem to get better over time. It's a little suspicious.”

“There's huge room for improvement in reporting in the industry.”

“The proof of the pudding is in the eating – we disregard the cash flow statement.”

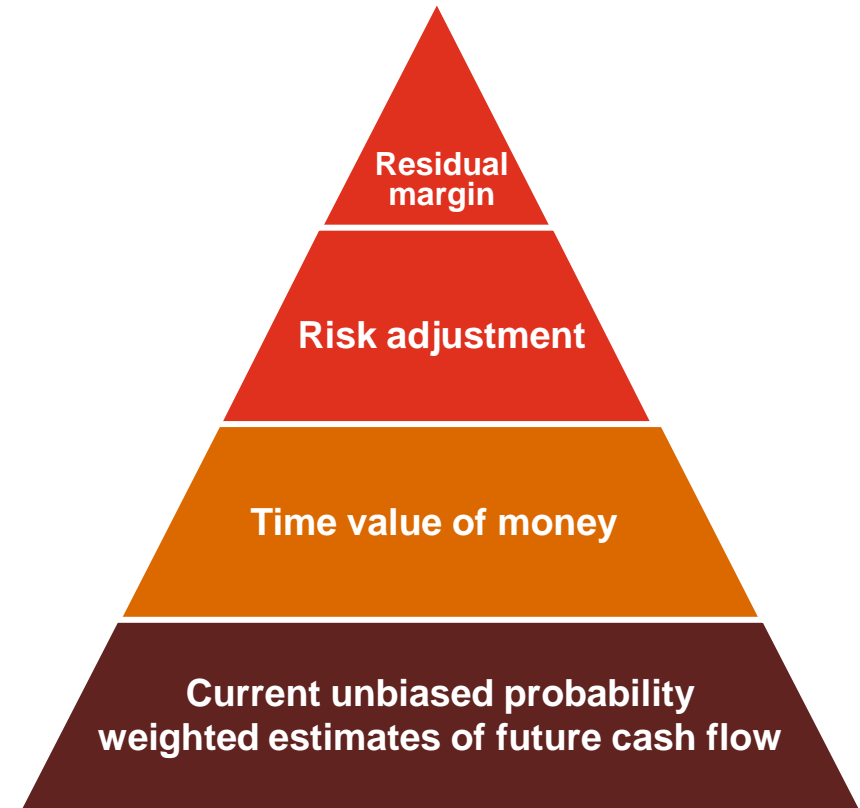
“The quality of reporting in the insurance industry certainly has an impact on valuations and also affects the amount of money going into the industry.”

“The income statement does not reflect the reality of the business.”

IFRS for Insurance Contracts

Measurement model – reminder

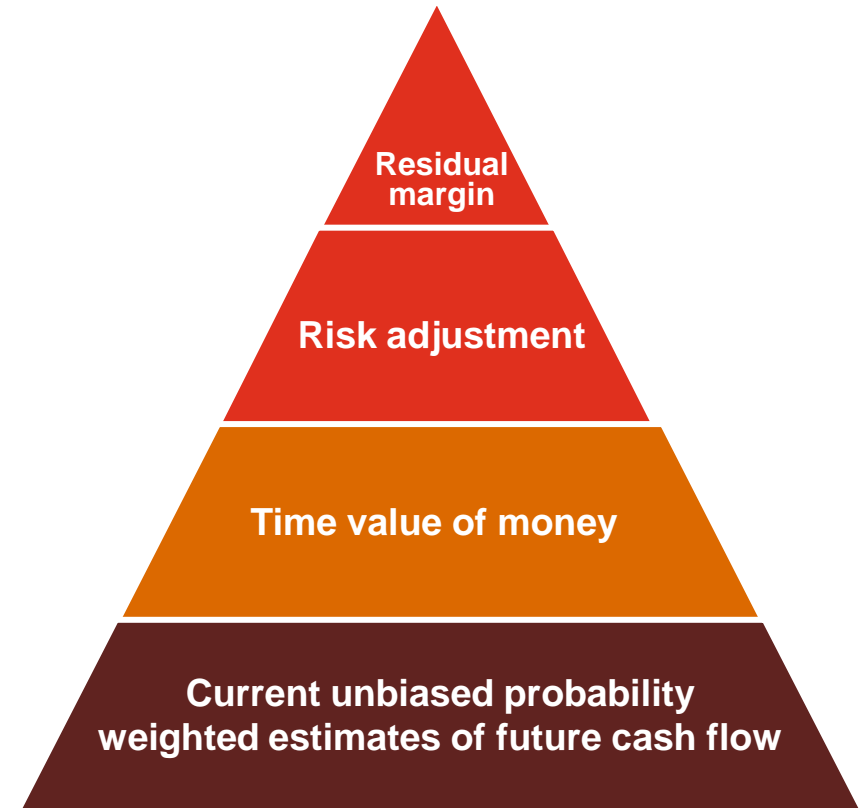
- Fulfilment rather than an exit objective
- One model for all insurance contracts
- Combination of rights and obligations (inflows and outflows)
- Day 1 loss in income statement, no day 1 gain
- Margins are part of liability
- Monetary item under IAS 21



IFRS for Insurance Contracts

Measurement model – reminder

- X** amount initially recognised is unwound but not remeasured
- ✓ updated for current estimates
- ✓ updated for market rates
- ✓ updated for current estimates



IFRS for Insurance Contracts

Presentation– reminder

| | Inception 1 January | Six month to 30 June | Six months to 31 December |
|---------------------------------|--------------------------------|---------------------------------|--------------------------------------|
| Change in risk margin | | 21 | 26 |
| Residual margin | | 13 | 13 |
| Underwriting margin | - | 34 | 39 |
| Acquisition costs | 10 | - | - |
| Experience adjustments | | (10) | (10) |
| Changes in estimates | | (20) | 0 |
| Net gain at inception | - | 0 | 0 |
| Investment income | | 40 | 38 |
| Interest on insurance liability | - | (25) | (23) |
| Profit/(Loss) | (10) | 19 | 44 |

IFRS for Insurance Contracts

Disclosure – reminder



- Retains IFRS 4 and IFRS 7 requirements
- IFRS 4 disclosures are lengthy and onerous
- Additional reconciliations
- Methods and inputs used in estimates

IFRS for Insurance Contracts

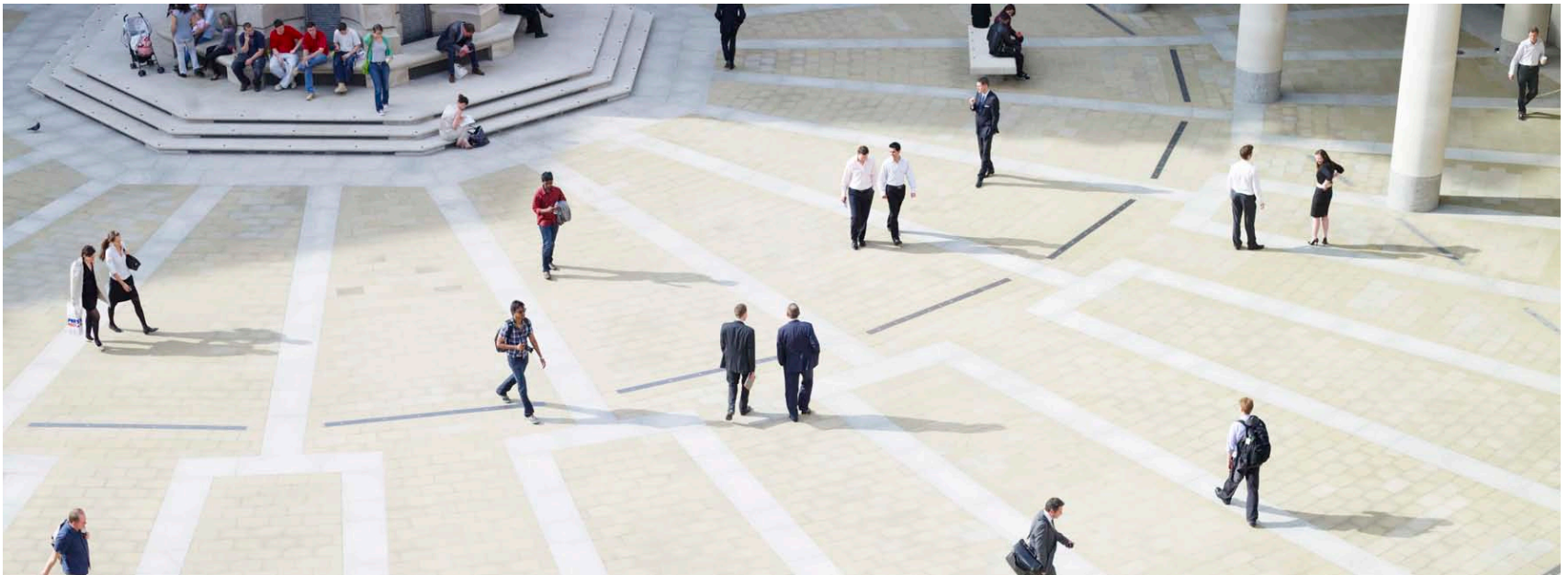
Likely changes in new Exposure Draft

- Flexibility in determination of discount rate
- Adjustment of residual margin prospectively
- Acquisition costs – portfolio level
- Contract boundary level wording – exclude contracts where there is an ability to reprice at a portfolio level
- Contracts recognised when coverage begins
- Unbundling of embedded derivatives
- No longer a day 1 gain on reinsurance contracts

IFRS for Insurance Contracts

Differences to FASB proposals

- **Explicit risk adjustment vs single composite margin**
- **Deferred acquisition costs**
- **Unlocking of margins for changes in cash flows**



IFRS for Insurance Contracts

Items to be finalised

- Calculation of risk adjustment
- Premium allocation approach for short duration contracts
- Presentational matters e.g. use of “other comprehensive income”
- Investment contracts with discretionary participating features
- Calculation of residual margin on transition
- Certain aspects around reinsurance
- Disclosures

IFRS for Insurance Contracts

Implications

- Impact on financial statements will vary for entities depending on nature of contracts and current local GAAP
- Likelihood of increased volatility since measurements reflect current estimates
- Profit recognition on transition for existing contracts
- Measuring and communicating business performance
- Practical implementation issues (e.g. definition of cash flows, discount rate, risk margin, scope of stochastic modelling)
- Need for new systems and data and related staff training
- Product design
- Relationship with regulatory requirements and tax

IFRS for Insurance Contracts

What do I need to do now?



- Continue to monitor debate
- Comment on new exposure draft?
- Identify the main impacts of the proposals
e.g. implications for KPIs
- Start considering an outline for a transition plan
 - resources
 - data available
 - systems needs

Solvency II Update

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Solvency II - Drivers

Solvency II for Insurers

What it delivers

- Risk and capital framework for insurers
- Harmonisation of requirements across EU
- Principles-based Directive supported by Levels 2 and 3 Implementing measures

Three-pillar approach

- P1 – quantitative requirements
- P2 – qualitative requirements
- P3 – disclosure requirements

Current status

- Level 2 implementation measures – consultation and finalisation
- Level 3 implementation measures – pre-consultation
- Quantitative impact studies
- Internal model approval

Solvency II – Where are we now?

Solvency II for Insurers

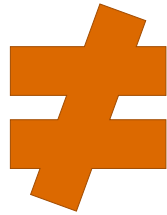
- Initial “go live” on 1 January 2013
- Latest Presidency compromise text for Omnibus II published on 21 June proposes:
 - delay to the implementation of until 1 January 2014
 - transposition the Solvency II directive into national law by 31 March 2013
 - certain requirements to be implemented by 1 July 2013 for the purposes of assessment only e.g.:
 - i. classification and approval of own funds
 - ii. approval of partial and full internal models
 - iii. use of undertaking specific parameters
 - iv. SPVs
 - v. calculation of group solvency requirements

Solvency II - Implications for insurance industry

- **Change to competitive landscape impacting the strategic, operational and corporate plans for all insurers regardless of specialism, location or scale**
- **Introduces considerable operational and structural challenges for many companies**
- **Removes regulatory arbitrage – maximum harmonisation across Europe**
- **Delivers business benefits through improved and more transparent governance, risk management, risk/reward balance and overall business controls**

Solvency II - Similarity with IFRS

IFRS



Solvency II

But it is close in some ways...

- Similar building block approach for insurance contracts
- Covers all the business that IFRS does
- Has allowance for an illiquidity premium
- Involves many similar disclosures
- Will use substantially similar data

Solvency II - Similarity with IFRS

Don't dig the road
twice!

Other regulatory matters

3

Enforcement strategy 2011 - 2012

“Regulated firms can expect increased enforcement activity, based upon our existing powers, new powers under the Central Bank Reform Act 2010 and additional enforcement powers proposed for 2011”.

- Improving effective compliance through the robust application of enforcement powers
- Enforcement activity prioritised in accordance with the risk profile of the financial institution
- Increased focus on persons involved in the management of financial institutions

Corporate Governance Code

Corporate Governance Code for Insurers

- Minimum standards of corporate governance
- Additional requirements for ‘major institutions’
- Minimum number of Directors
- Role of Non-Executive Directors
- Limits on number of directorships
- Tri -annual review of Board composition
- Establishment of audit and risk committees
- Annual compliance statement to Central Bank
- Applies from 1 January 2011 (grace period of 6 months)

Corporate Governance Code

Corporate Governance Code for Insurers – guidance on FAQ

Guidance reflecting answers to questions which have been raised in relation to the Code

- Criteria for determining whether a director is independent
- Reporting of “material deviations” from the Code to the CBI
- Limits on number of directorships (cumulative, scope for exceptions)
- Review of Board membership and performance (format, external evaluator suitability)
- Board committees (membership, meetings attendance, extent of reliance on sub-committees)
- Format of the compliance statement

Hub and spoke principles

- New supervisory model for the hub and spoke structures
- Opt in/opt out options given to all host EEA regulators of significant branches
- Legal entities at the hub must demonstrate how the oversight is achieved
- Roles and responsibilities of the hub (head office) and spokes (branches) should be clearly outlined
- Firms required to sign-up to the principles in a prescribed format

Hub and spoke principles

Principle 1:

Governance should be aligned and oversight assigned to the hub

Principle 3:

Management information should reflect an appropriate balance between financial performance and risks and controls

Principle 2:

A high priority to be assigned to risk management at the firm's head office

Principle 4:

Minimum standards for controls over outsourcing activities

Consumer Protection Code

Changes to the Consumer Protection Code

- More prescriptive Know Your Customer requirements
- More rigorous suitability requirements
- Enhanced disclosure and transparency requirements
- New definition of a “vulnerable” customer
- Requirement to identify nature and extent of risk inherent in new products
- New requirements for assessing affordability, including income verification and stress testing
- More prescriptive requirements on handling of errors

Fitness & Probity

New Fitness & Probity regime for financial services industry

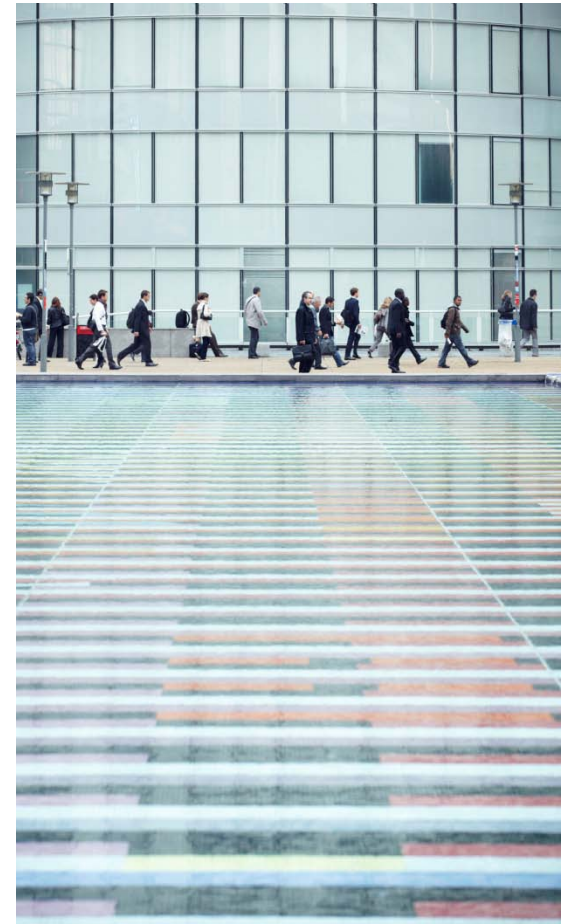
Part 3 of the Central Bank Reform Act, 2010

- Enhanced fitness & probity regime applicable to individuals across all regulated financial services providers
- Operating details for the Control Functions (CFs) and Pre-Approved Control Functions (PCFs) i.e.:
 - List of persons in CFs and PCFs to be maintained
 - Display due diligence to prove Fit & Proper compliance
 - Statement of Compliance to the Central Bank
- Definition of “Fit & Proper”
 - Competent and capable
 - Honest, ethical and acting with integrity
 - Financially sound

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Auditor Protocol (Consultation)

- Framework for CBI and auditing profession to share “relevant information”
- Bi-lateral and tri-lateral meetings
- Legislative and other implications
- Consultation closed 23 September 2011



Insurance Breakout Session

Insurance Banana Skins 2011

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Insurance Banana Skins 2011

Top risks identified

- Identifies risks facing the global insurance industry as seen by global sample of nearly 500 practitioners
- Top 5 risks in 2011:
 1. Burden of regulation (up from No. 5)
 2. Scale of new capital requirements (up from No.3)
 3. Uncertain macro-economic trends (up from No.4)
 4. Investment performance (down from No.1)
 5. Natural catastrophes (up from No. 22)

New risk identified in 2011: TALENT

Insurance Banana Skins 2011

Changes since 2009 (2009 ranking in brackets)

1. Regulation (5)
2. Capital (3)
3. Macro-economic trends (4)
4. Investment performance (1)
5. Natural catastrophes (22)
6. Talent (-)
7. Long tail liabilities (10)
8. Corporate governance (17)
9. Distribution channels (16)
10. Interest rates (11)
11. Political risk (18)
12. Actuarial assumptions (9)
13. Managing costs (14)
14. Management quality (13)
15. Risk management (6)
16. Reputation (15)
17. Back office (24)
18. Retail sales practices (25)
19. Complex instruments (8)
20. Climate change (28)
21. Reinsurance (20)
22. Fraud (23)
23. Terrorism (26)
24. Product development (29)
25. Pollution (34)
26. Managing mergers (31)

Thank you

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