



4 June 2009

Mr. Carlos Montalvo Rebuelta
Secretary General
CEIOPS
Westhafen Tower
Westhafenplatz 1
D-60327 Frankfurt Am Main

Ref.: *CEIOPS-CP-26-09*

Our Ref.: INS/HvD/LF/SR

Dear Mr. Montalvo Rebuelta,

Re: FEE Comments to CEIOPS on Consultation Paper No. 26 Draft CEIOPS' Advice for Level 2 Implementing Measures on Solvency II: Technical Provisions – Elements of actuarial and statistical methodologies for the calculation of the best estimate

- (1) FEE (the Federation of European Accountants) is pleased to provide you below with its comments on the CEIOPS Consultation Paper No. 26 Draft CEIOPS' Advice for Level 2 Implementing Measures on Solvency II: Technical Provisions – Elements of actuarial and statistical methodologies for the calculation of the best estimate (“the Paper”).

General comments

- (2) Most of the Paper deals with the actuarial techniques to determine the “best estimate”. It is not our intention to provide detailed comments on the actuarial content of the paper and we have focussed our comments on those aspects of the paper that may be interrelated with financial reporting.
- (3) Our understanding of the current discussion of the IASB phase II project on Insurance Contracts is that the estimation of the expected value (or mean value of discounted cash flows) under IFRS would be the same as the calculation of the best estimate for the purposes of Solvency II. Furthermore, we expect that companies preparing their financial statements in accordance with IFRS will be allowed to use the calculation for the financial statements for the calculation of their technical provisions for Solvency II.

- (4) Therefore, we would be concerned about having a definition or detailed prescription for the calculation of the technical provisions in the Level 2 implementing measures since this may lead to conflicts with the calculation required for financial reporting purposes. On this basis, we would advise CEIOPS and the European Commission to consider limiting the guidance in Level 2 at this stage to the underlying principles for the selection of valuation techniques.
- (5) Generally, the Paper promotes simulation techniques which require the assumption of a distribution function. Where there is no distribution of possible outcomes available, it is debatable whether such simulation techniques are sufficiently verifiable so that they can be accepted for external reporting purposes. We believe that in these circumstances, the techniques should not apply for Solvency II purposes either. On the other hand, we note that the analytical approaches that companies may apply to estimate expected cash flows for financial reporting purposes should be acceptable for Solvency II purposes.

Detailed comments

Paragraph 3.1.:

- (6) We do not believe, "... that the best estimate shall allow for uncertainty in the future cash-flows". The best estimate should be an unbiased measure. As stated in paragraph 3.1 of the Paper, the best estimate comprises the probability weighted average of future cash flows, adjusted by the risk free rate. The probability weighted average of future cash flows is just that, a simple average based upon the probability of certain outcomes. It is not adjusted to reflect the potentially variability in the range of potential outcomes. Uncertainty over future cash flows is dealt with separately through the risk margin.

Paragraph 3.9./3.30.:

- (7) We note the recommendation in paragraph 3.30 of the Paper that the supervisor "shall be required to require an alternative valuation technique where that other valuation technique achieves the objective of the valuation (prudent, reliable, and objective) in a better way." We do not agree that the objectives of the best estimate should include prudence since the best estimate should be an unbiased measure as noted in our comments about paragraph 3.1 of the Paper (see above in paragraph 6 of this letter).

- (8) We agree that, where the objectives of financial reporting do not meet supervisory needs, measurement techniques for regulatory purposes may deviate from those for financial reporting. We question whether this should be the case when calculating the best estimate, since the basis of both financial reporting (based on current thinking on the IASB's Phase II standard on Insurance Contracts) and prudential supervisors should be for an unbiased best estimate, onto which a risk margin will then be applied.
- (9) We note that Article 37 of the "Framework Directive" sets out circumstances under which capital add-ons may be applied by supervisors. We are not convinced that the draft advice in paragraph 3.30 of the Paper meets the criteria in Article 37. We believe it would not be appropriate to specifically authorise supervisors to require an alternative technique for assessing best estimates. Where an insurer applies the same valuation techniques for financial reporting and solvency purposes authorising the supervisor to require an alternative technique may increase uncertainty and create doubt about the figures reported in the audited financial statements.

For further information on this letter, please contact Ms. Saskia Slomp from the FEE Secretariat.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Hans van Damme', with a long, sweeping horizontal line extending to the right.

Hans van Damme
President