CFO FORUM

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Solvency II Working Group
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9 June 2009

Dear Sir / Madam

CFO Forum responses to:
CEIOPS Consultation Paper 35: Valuation of Assets and "Other" Liabilities

Please find attached the CFO Forum's response to CP 35.

Thank you for extending the deadline slightly in order for us to be able to communicate effectively will the members of the CFO Forum on the more complex items covered by this consultation paper.

Yours sincerely

Amélie Breitburd
Chair
CFO Forum, Solvency II Working Group

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Please insert your comments in the table below, and send it to secretariat@ceiops.eu in Word format. In order to facilitate processing of your comments, we would appreciate if you could refer to the relevant section and/or paragraph in Consultation Paper 35-09.	
Reference	**Comment**
General comment	**IFRS as a reference framework –** whilst the CFO Forum supports the use of IFRS as a reference framework for the Solvency II balance sheet (or alternative frameworks e.g. USGAAP, where it is substantially equivalent to IFRS), IFRS does not always provide an economic valuation for all assets and liabilities. Solvency II should carefully consider references to IFRS when the appropriate IFRS standard is not based on sound economic principles. **IFRS Fair Value -** we agree that assessing assets and liabilities should be based on a sound economic basis and that Level 1 text's main principles applicable to valuation of assets and liabilities largely coincide with the current definition of fair value under IFRS with the notable exception of the treatment of own credit standing for liabilities and the burden of proof and presumptions related to current prices as the best evidence of fair value when measuring financial assets not currently quoted in an active market. As a general rule, it should be the case that a value recognised as a fair value under IFRS is also recognised as an economic value under Solvency II. This must also apply to fair values disclosed in the notes which complement balance-sheet items which are not recognised at fair value. Consequently, we also concur with the use of the fair value proposed hierarchy for the valuation of assets ranging from mark to market to mark to model as outlined under IFRS, but point out the difficult application of some of the provisions of the application guidance developed by the IAS 39 IASB Expert Advisory Panel in October 2008. We draw attention to the IASB's "Fair Value Measurement" project described below. For the purpose of constructing the Solvency II balance sheet we consider

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	that the basis for mark to market and mark to model valuations in Solvency II should permit all valuations that are defined as fair value in IFRS without further adjustment (subject to the required valuations being required for the same underlying resources). **Fair valuing financial assets and other items of the Solvency II balance sheet –** the CFO Forum starting point is our commitment to measure the Solvency II balance sheet on a market consistent basis while learning lessons from the current crisis. This is to ensure that Solvency II valuations are appropriate in a wide range of economic scenarios and therefore avoid pro-cyclical effects. In this context, the valuation of each item of the balance sheet, in order to be consistent, while measuring each component separately should take into account current market conditions. The measurement of technical provisions is out of the scope of this consultation paper, however, sound economic principles should apply consistently to the technical provisions as well as all other items on the economic balance sheet. Our comments are based on the assumptions that technical provisions measurement will be based on economic principles and should not be taken in isolation from our other responses to level 2 implementation measures consultation papers. **Audited financial statements and materiality -** we encourage CEIOPS to rely on audited financial statements when they are a source of fair values which are economic values in terms of solvency II. It is not clear how significant the difference between the financially reported amount and the economic value should be before an adjustment is required. The principle of proportionality does not define guidelines of materiality. For the purpose of constructing the Solvency II balance sheet we would support the use of IFRS materiality principles, subject to the requirement that adjustments should be made where their value would have a material impact on risk adequacy within the SCR calculation. Consistent with the principle of proportionality it should be unnecessary to estimate assets and "other" liabilities on an economic basis where the difference in value is not material or would be materially off set by the increase in risks capital requirements if the additional value was included in the economic balance sheet. **Supervisory review process -** a harmonised basis of review of economic balance sheets is required. **Estimation of market values** - valuation should generally be based on the application of appropriate market measures including mark to model techniques. For example, a life insurer may use it internal economic capital model to measure the defined benefit pension liabilities of its employees, which may give a better market value of these liabilities than IAS 19. Mark to model approaches apply across Solvency II, not only to the measurement of the Solvency II balance sheet and the general approach should be defined once to apply universally across Solvency II. In this context we highlight that mark to model approaches do not seek to minimise the use of unobservable inputs but instead use entity specific assumptions where

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	relevant and reliable observable market inputs do not exist. **Changes to IFRS** - as mentioned above a fair value from IFRS in general should qualify as an economic value under Solvency II. Changes in IFRS should not alter that fact. Additionally there are a number of IASB projects underway, which directly affect the present consultation paper, including: 1. Fair value definitions of IFRS are currently reviewed in the IASB's project "Fair Value Measurement". The Board is developing an exposure draft of an IFRS on fair value measurement guidance which it plans to publish this quarter already. This project is still open to discussion and we recommend that CEIOPS revisits its advice on using and adjusting IFRS valuations when the IASB has reached its conclusions on this project. 2. Revisions to IAS 37 are expected to be published before the end of 2009. Current proposals suggest that a revised IAS 37 will not recognise the concept of contingent assets and contingent liabilities, referring instead to all assets and liabilities. The IASB has not reached its final conclusions on this project so we recommend that CEIOPS revisits its advice on using and adjusting IFRS valuations when the IASB has reached its conclusions on this project **Interpreting IFRS valuations should be in level 2, not level 3, and should be reviewed when new standards are published** - all advice on interpreting IFRS valuations in the context of Solvency II should be contained in the level 2 implementing measures to avoid inconsistent application by territory due to variation in level 3 supervisory guidance, which should be restricted to advice on interpreting local GAAP accounting valuations, if required. Due to the number of projects the IASB is currently working on and the potential significance of the changes to current standards the CFO Forum recommends that the need to change the level 2 implementing measures is reviewed each time the IASB publish a new standard. **Economic values reflect inherent uncertainties and do not require further adjustment -** the CFO Forum firmly believes that economic values incorporate all risks relevant for that valuation. Additional uncertainty attaching to risks inherent to the assets and liabilities being valued should be allowed for in the SCR calculation. Valuation and risk capital requirements must not be mixed.
Section 3 – heading b	**"Methodology for determination of economic values"** - The headline should make clear, that the following descriptions are referring to the valuation of assets only. As a general rule, it should be the case that a fair value recognised as a fair value under IFRS is also recognised as an

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	economic value under Solvency II. This must also apply to fair values disclosed in the notes on the balance-sheet items which are not recognised at fair value.
Para 3.22	**IFRS as a reference framework for Solvency II balance sheet valuations** - we support CEIOPS´ proposal to use IFRS endorsed within the EU as a reference framework for building an economic balance sheet under solvency II principles (or alternative frameworks e.g. USGAAP where it is substantially equivalent to IFRS). As a general rule, it should be the case that a value which has been recognised as a fair value under IFRS should also be recognised as an economic value under Solvency II except when the appropriate IFRS standard is not based on sound economic principles. We should state that IFRS does not only cover the valuation of balance sheet items, but also the recognition of certain items in the balance sheet. Whilst recognition and derecognition of insurance liabilities and own funds will need to be considered for Solvency II in separate consultation papers, we recommend that for other assets and other liabilities the IFRS principles for recognition and derecognition should be applied.
Para 3.23	**Level 2 implementing measures should cover all key aspects of valuation of assets and liabilities –** this is necessary to avoid variation in application through level 3 guidance. In particular the level 2 implementing measures should explain when IFRS valuations can be uses as a proxy such that the guidance will continue to be relevant as IFRS changes. IFRS should be used as a proxy when the IFRS valuation is defined as fair value in or when the described valuation is equivalent to economic value on a mark to model basis. **Level 3 supervisory guidance should not cover use of IFRS valuations -** in order to avoid inconsistent application of IFRS to Solvency II, level 3 supervisory guidance, should be restricted to advice on interpreting local GAAP accounting valuations, if required. The IASB has a number of projects underway to change existing standards or introduce new standards and some of these will directly affect the present consultation paper. The CFO Forum recommends that the need to change the level 2 implementing measures is reviewed each time the IASB publish a new standard, taking into account the appropriateness of the new IFRS standard and its consistency with sound economic principles.

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Para 3.24	**The CFO Forum agrees with this paragraph except** that we anticipate that for some balance sheet items (e.g. receivables and payables) the waiver of an adjustment will for most companies be adequate without violating the Solvency II principle of proportionality. We therefore recommend the deletion of the words "*exceptional situations"* in reference to the materiality of adjustments of IFRS valuations.
Para 3.25	**Economic value will reflect inherent uncertainties** - we do not agree with CEIOPS' proposal. If an asset is valued at its economic value this will already take account, to the appropriate extent, of all risks which arise from holding that asset and the value will not require a further adjustment. Additional risks should be considered in the SCR rather than by "redefining" the economic valuation. Mixing approaches makes calibration rather difficult and would perhaps not result in a proper understanding of the solvency and financial condition of the undertaking. We would request the text "*or adjustments to the economic valuation*" be removed.
Para 3.26	**Mark to market approach** - we agree; see comments on section 1 above
Para 3.27	**Mark to model approach** - we agree when marking to market is not possible, a mark to model approach should be used. Mark to model approaches apply across Solvency II, not only to the measurement of the Solvency II balance sheet and the general approach should be defined once to apply universally across Solvency II. In this context we highlight that mark to model approaches do not seek to minimise the use of unobservable inputs but instead use entity specific assumptions where relevant and reliable observable market inputs do not exist.
Para 3.28 - 3.30	**Governance** - issues concerning system of governance should be dealt within together and not as ad hoc additions to measurement guidance. These paragraphs should be deleted. **Economic values reflect model** uncertainty - the concept of *"valuation adjustments"* in Para 3.29 is not acceptable. The text states *"Valuation adjustments should be made as appropriate, for example to cover the uncertainty of the model*

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	valuation": this is in contradiction with the economic value principles (see comments to para 3.25 for discussion) and should be deleted.
Para 3.31 – 3.32	**Internal opinions should be permitted -** it is unclear whether the requirements for external, independent verification of valuations in a number of circumstances are in addition to the external auditor's statement. We do not support any requirement for additional external, independent verification of valuations. All valuations at fair value in the financial statements are covered by the external auditor's opinion. Where balance sheet items require material revaluation to estimate an economic value, we would support the requirement for an independent verification of the valuation, which could be conducted by either an internal or an external independent expert. This independent verification should consider both the appropriateness of the valuation basis to determine economic value and an explanation of the reconciliation to the audited amount. **The frequency of independent value verification should be proportionate to the material variability of the value.** Some items experience significant and volatile changes in economic value whilst other items with only experience insignificant changes in economic value. The CFO Forum recommends that when a value is based on IFRS, the frequency of independent revaluations should be consistent with the IFRS requirements in the relevant standard. Where the IFRS valuation is adjusted for Solvency II purposes the frequency of independent revaluation should take into account the materiality of the variability in that adjustment consistent with the principle of proportionality.
Para 3.33	**Fair-value measurement in line with IFRS includes those risks which impact market value.** At the same time, the risk-capital requirement for the SCR is defined separately and comprises those risks which are not expected (variance). Mixing these two concepts is not conducive to the objectives here. Additional risk adjustments should not be made to the fair value. The particular risks mentioned should be considered within the SCR calculation. We consider that there are not any additional risks that are not already reflected within the market price or in the calculation of the variance of the underlying asset value/return. In detail: • First bullet point of Para 3.21: the paragraph points out the need for assessing the *"illiquidity of the asset due to entity specific constraints".* We disagree with this valuation adjustment, since we believe that the illiquidity of assets is already taken into account in the valuation of the asset. Also; the illiquidity risk is already taken into account in the concentration

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	risk. Thus, we recommend this bullet point be removed from the CP. • Second bullet point of Para 3.21: even though we consider the need for addressing the *"inherent* un*certainty linked to the use of models for the of models for the determination of economic value"* as a fair concept, we recommend that the CP details the specific situations where these valuation adjustments occur, and the way to reflect it in the fair value. We believe that the internal or external models used to assess the value are already embedding the uncertainty. As such we propose to remove this bullet point also.
3.41 – 3.42	**Goodwill on acquisitions** We do believe goodwill has economic value but we recognise and agree the challenges with its recognition for solvency purposes. If it were to carry a value on the solvency balance sheet, then goodwill should draw an appropriate capital charge.
Para 3.47- 3.48	**Intangible assets** The CFO Forum does not agree with the conclusion that only intangible assets that are measured at fair value in accordance with IAS 38 should be deemed as having economic value under Solvency II. According to IAS 38, the balance sheet value for all intangible assets must be annually verified. This implies that intangible assets measured at cost should be written down if the annual impairment test calculating the fair value results in a lower value than the cost value. In practice, there are intangible assets that may be sold where an active market does not exist, for example licenses or software, for which reasonable valuations can be obtained. It seems inconsistent to require insurers to measure certain assets at market value where no active market exists (for example, investment property), but not others (such as intangible assets). The risks associated with the intangible assets should be considered within the capital requirements, not a reduction in the economic valuation.
3.60-3.63	**Property, plant and equipment**
Para 3.61	**Use of a revaluation model should be proportionate** - we agree that the revaluation model may be appropriate for owner-occupied property. However, imposing a revaluation model on plant and equipment, should this be immaterial, is not consistent with the principle of proportionality. IAS 16 proposes a pragmatic valuation hierarchy that allows for circumstances

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	when there is no market based evidence of fair value. The CFO Forum recommends that Solvency II permits unadjusted IAS 16 valuations for property, plant and equipment.
Para 3.62	**Internal opinions should be permitted -** expert opinions should suffice, even if prepared internally. **Frequency of independent revaluations should be consistent with IAS 16** – consistent with the principle of proportionality; the frequency of independent revaluations for Solvency II should reflect the materiality of the variability of those valuations. For items where values vary immaterially an independent valuation at least every three years is unnecessarily onerous. The points made in relation to paragraphs 3.31 and 3.32 also apply here.
Para 3.63	**Consistent principle for disclosures to supervisors are required** - the disclosure of information, on request of the supervisor, concerning the methodologies used on (re)valuation appears to be in line with the (future) pillar 3 requirements under Solvency II. We recommend that disclosures to supervisors are developed under a consistent set of principles that apply to the entirety of Solvency II, rather than on an ad hoc basis attaching to different elements of valuation. We propose that paragraph 3.63 is deleted.
3.70-3.72	**Investment Property**
Para 3.70	The application of IAS 40 (fair value model) appears to be a suitable proxy for solvency purposes. Where investment property is currently measured at cost, the requirement to revalue at an economic value should be in line with overall materiality in accordance with the principle of proportionality.
Para 3.71	**Internal opinions should be permitted -** expert opinions should suffice, even if prepared internally. **The frequency of independent value verification should be proportionate to the material variability of the value.** There should be no requirement to obtain independent revaluations where the change in the economic value will be immaterial

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	since the previous valuation. Consistent with comments on 3.31, 3.32 and 3.62.
Para 3.72	**Consistent principle for disclosures to supervisors are required** - the disclosure of information, on request of the supervisor, concerning the methodologies used on (re)valuation appears to be in line with the (future) pillar 3 requirements under Solvency II. We recommend that disclosures to supervisors are developed under a consistent set of principles that apply to the entirety of Solvency II, rather than on an ad hoc basis attaching to different elements of valuation. We propose that paragraph 3.72 is deleted. Consistent with comments on 3.63.
General Comments on paras 3.78 – 3.85	**Participations/associates, subsidiaries and joint ventures, SPVs** **The treatment of participations in SII should be considered in a holistic manner** – We understand that this consultation paper deals only with the valuation of participations at solo level. However, participations need to be considered in the wider context, also taking into account own funds and the consolidation of non insurance participations in group accounts. **Definition of participations** – Solvency II should permit the same definition of participations as permitted in IFRS rather than applying the 20% threshold. Further in defining participations for solo entities, insurance groups regulated under Solvency II should consider the total group participation and treat all solo participations consistent with the overall group participation. **Participation valuations** – participations should be measured based on market values or value in use on a look through basis. This is consistent with economic valuations and the Directive defining the values of assets and liabilities as those that an insurer would have to pay or receive if it was to transfer its assets and liabilities immediately to another insurance or reinsurance undertaking.
Para 3.83 and 3.85	**Special Purpose Vehicles** If an SPV fulfils the criteria for a “participation”, its corresponding equivalent treatment is a given.

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	Where an entity holds retained interests or other investments in an SPV that SPV will not appear on a solo entities balance sheet. It might, however, be included in group balance sheet.
Para 3.94	**<u>Financial assets</u>** We agree with measurement of financial assets at fair value as defined in IAS 39 but point out the difficult application of some of the provisions of the application guidance (for example, the burden of proof and the presumptions related to current prices as the best evidence of fair value when measuring financial assets not currently quoted in an active market).
Para 3.103 – 3.104	**<u>Contingent Assets and Liabilities</u>** The current version of IAS 37 is not considered to be consistent with economic value under Solvency II or the IASB's current thinking on Fair Value. A revised version of IAS 37 will be published in Q4 2009. Revision to IAS 37 are still open, however, the current proposals suggest that contingent assets and liabilities are no longer defined terms for financial reporting purposes. The CFO Forum recommends that the Level 2 implementing guidance should be revisited to reflect the new IAS 37 definitions and measurement proposals when the revised standard is published.
General Comments para 3.117-3.122	**<u>Deferred Tax Assets and Liabilities</u>** The IASB issued in March 2009 an exposure draft on Income Tax that would lead in some cases to changes in the recognition/measurement of current and deferred taxes for which the economic value could be questioned (i.e. recognition of a deferred tax liability for all temporary difference associated with investments in domestic subsidiaries even if a payment of dividend or a sale of the investment is not probable). The deferred tax assets and liabilities calculated in accordance with IAS 12 for financial reporting purposes will not necessarily be a proxy for the deferred tax assets and liabilities in the Solvency II balance sheet as the value of the assets and liabilities underlying the deferred tax calculation may have changed in value from an IFRS basis to and economic value for Solvency II. Deferred tax assets and liabilities for Solvency II purposes should be calculated based on the principles in IAS 12. Where the financial reported deferred tax value would not materially different if calculated on a Solvency II basis the financial reported

	number should be regarded as a reasonable proxy.
3.117	**Valuation of deferred tax assets and liabilities should be linked to identifiable and expected future assets and liabilities** - we do not agree with the idea that deferred tax assets or liabilities shall be linked with identifiable assets or liabilities on the Solvency II balance sheet. This is contrary to the Solvency II economic principles (as well as contrary to IAS12 principles). Under a Solvency II perspective, the only consideration for recognition and measurement of deferred tax assets and liabilities should be their recoverability or their probability of payment (respectively). Level 2 implementing measures should be consistent with the proposed definition of deferred tax in the IASB's exposure draft, namely that deferred tax is income tax payable or recoverable in future reporting periods in respect of the taxable profits or losses arising from past transactions or events. It is more appropriate to consider deferred tax assets on tax losses as a tax receivable rather than a deferred tax. The economic valuation of these assets should reflect the probability of receipt consistent with the requirements of Solvency II.
3.118	**Unused tax losses and tax credits should be evaluated on an economic basis -** we do not agree with a valuation of nil. In principle the unused tax loss can be directed back to a valuation movement in a specific asset or liability. The deferred tax asset will therefore have an impact on the overall economic value and should be reflected in the balance sheet. Furthermore in our opinion the recognition of the unused tax losses should be based on the recoverability principle (as per our comment to Para 3.117). If an insurer is able to demonstrate that is it is able to use the unused tax loss either by means of a carry back or a carry forward, it should be allowed to recognise the value of the unused tax loss. Furthermore: • the suggested approach could create some differences between available capital under Solvency II and equity under IFRS; • it could have unwanted effects on available capital. • tax losses are often valued in transactions of insurance companies because they increase the net cash flows from the investment so although they are not assets that can be sold separately from the company (or business of the company), they do have an economic value if the whole company (or business) is sold.

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	CEIOPS' departure from IAS12 has not been sufficiently justified with a set of solid and clear arguments. While IAS 12 attributes explicitly an economic value to those assets under certain conditions. CEIOPS doesn't explain why those particular deferred tax assets that are recoverable would be intrinsically different to a general deferred tax asset (a general calculation of deferred taxes may result a deferred tax asset in a Solvency 2 balance sheet) and then would require a specific treatment. The fact that unused tax losses or tax credits are not linked to specific assets or liabilities of the Solvency 2 balance sheet (see para 3.117) should not prevent one from considering them as assets with a positive economic value. Indeed, the fact that there is no specific asset within the balance sheet is contradictory with the principle of the temporary difference. When a company has an unused tax loss, it has an asset on a taxable basis. This can be the case for any temporary difference, where the asset does not exist for accounting or solvency purposes, but does exist for tax purposes. Hence if revenue has already been taxed and that tax may be recoverable in future periods the economic value of this asset should be reflected in the Solvency II balance sheet. This economic value is the result of the recognition (under the IAS 12 provisions) that these deferred tax assets can be recovered thanks to existing deferred tax liabilities, such as calculated in the Solvency 2 balance sheet or, in their absence, thanks to future positive tax bases calculated on a prudent "on-going concern" basis. Recognition principles for deferred tax assets are already very restrictive, in particular where there is a history of losses. When losses are unusual, however, and can be estimated reliably, there is no valid reason to consider that the deferred tax asset has no economic value. Deferred tax assets may offset deferred tax liabilities to some extent. A company that is carrying deferred tax liabilities in its Solvency II balance sheet whereas the tax credits or the unused losses are not recognised will not present a fair tax position regarding assets and liabilities. This is because at least some of the deferred tax liabilities will be offset against the tax credits or unused tax losses and will never be charged as current tax liabilities. It would also be helpful if some guidance was provided on how tax losses should be incorporated into required capital calculations. Loss events that are modelled in the required capital calculations will create tax losses that have an economic value because they reduce tax liabilities on subsequent profits. The loss absorbing properties of deferred tax assets should be appropriately reflected in the calculation of the MCR and SCR.

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Para 3.119 – 3.121	**We agree IAS 12 is an acceptable proxy** - regardless of the local tax base used and the final composition of the economic balance sheet, any adjustment from the local tax base to arrive at the economic balance sheet should result in a corresponding tax loss/credit on the Solvency II balance sheet. However, we should point out that this was not tested under QIS4. To avoid any misinterpretation, we would request that the text in paragraph 3.121 is adjusted as follows: "*The relevant deferred taxes for solvency purposes shall be determined by the differences between the economic valuation of an asset or liability,* <u>including technical provisions</u>, *on the Solvency II balance sheet and its tax base*". Entities regulated under Solvency II may be influenced not by a single tax regime but also by tax regimes applicable to international subsidiaries and branches, as local tax subjects, regardless of whether the regulated entity is tax exempted or not (tax credit).
Para 3.122	**Deferred tax assets should reflect the time value of money** - the CFO Forum believes that deferred tax assets should reflect the time value of money. If the IAS 12 basis for calculating deferred tax is applied to a company's economic balance sheet, the value of the assets and liabilities implicitly reflect the time value of money and no further discounting of the deferred tax asset is required. If, however, the deferred tax asset is based on the amount that will require payment to the tax authorities at a future date, that amount should be discounted to the balance sheet date.
General Comments para 3.124 – 3.140	**<u>Other financial liabilities and amounts payable</u>** **Valuation of liabilities** – Concerning liabilities which have been issued for financing purposes the discussion about what constitutes an economic value appropriate for a solvency balance sheet will run differently from a discussion about the economic value of assets, because the aim is to look at each entity's solvency position. **Own credit standing** - In transactions between third parties, a liability from a company with a very bad credit standing would have low value. This is what would be referred to as the market price. For an insolvent company the price of debt might approach nil. The insolvent company is, however, still liable to pay the nominal value of its debt. For the entity issuing the debt, the nominal value of the liability does not decrease in the way market prices would. When a company is known to

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	be in financial difficulties, however, it is easier for it to enter into arrangements with creditors that allow the liabilities to be discharged for an amount less than the nominal value of the debt. For the purpose of solvency regulation, a supervisor should be interested in the amount a company actually owes to its debtors. The failure to pay debts as they fall due will ultimately result in intervention under local insolvency laws. Thus the payable amount should be the primary consideration for supervisory purposes. Whilst the CFO Forum supports the view that an entities liabilities should not reflect own credit standing for Solvency purposes, some companies issue debt instruments that are actively and can be valued based on an observable market price. This price, however, would reflect the own credit standing of the entity. The CFO Forum would not require entities to apply explicit adjustments to observable market prices to remove the effect of own credit standing from such values in the Solvency II balance sheet. **Discounting for the time value of money** - since companies need to be able to pay their debts when they fall due, the valuation of those debts should reflect the time value of money until the company is required to repay the debt. Where there is no one fixed date the expected timing should be used. **The CFO Forum considers the different valuation schemes to be appropriate as follows:** **<u>Preferred approach: Market value at inception, fluctuation of market rates excluding own credit risk at subsequent valuation</u>** Initial measurement should be based on market value, which will reflect own credit standing of the debt at issue. Subsequent valuations should reflect changes in market values at subsequent valuation dates, subject to materiality. The CFO Forum considers that the economic value of liabilities should reflect the economic values of those obligations to the company which may differ from the economic value to a market participant. This approach permits the use of replicating portfolios. We highlight that the value of a replicating portfolio (unless otherwise adjusted) reflects the credit standing of the financial instruments used to determine the replicating portfolio and not the own credit standing of the liability being evaluated. **<u>Second best approach: Market value at inception, amortised cost at subsequent valuation</u>** This approach is desirable when there are no observable market values at subsequent revaluation dates or where the

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	adjustment required to reflect fluctuations in market rates is not material. An additional adjustment is made under IFRS, as transaction costs are regarded as financing costs and are distributed over the duration of the liability. To make it easier for the IFRS applicants, this relatively small adjustment which is included in amortised cost should also be accepted as part of an economic value under Solvency II. The rationale for this is that the received financing cash flow is being reduced by the cost incurred at inception and these costs are similar to interest payments being distributed over the term of the liability. **Not recommended: Approach 1 (use a risk free rate for valuation) or alternatively market values including fluctuating own credit standing** The CFO Forum considers that both valuations using a risk free rate only and valuations using rates including own credit standing at subsequent valuations are not suitable for a Solvency II balance sheet. **Other comments** **Amortised cost** - the statement in paragraph 2.126 is not correct. The amortised cost method means that liabilities will be recognised at market value less transaction cost at inception. In the following amortised costs lead to the liability approaching its nominal amount at the due date. **Own credit standing** – level 2 implementing measures should be clear that market values at inception reflect the credit standing of the liability which may differ from the overall credit standing of the entity due to priority of the debt or the existence of other guarantees. **Debt versus equity** - we note that the distinction between debt instruments and equity instruments is not discussed in this paper. We will discuss our position on this topic in response to the relevant consultation paper.
Para 3.145 - 3.155	**Post employment benefits** **Current IAS 19 is not a suitable proxy** for an economic valuation of all post employment benefits in many cases **The CFO Forum recommends that post employment benefits should be valued on an economic basis using an appropriate mark to model methodology that reflect the obligations of the entity**. IAS 19 valuations should be permitted as a proxy where the difference from an economic valuation would not be material. **Revisions to IAS 19** – the level 2 implementing measures should not pre-empt the improvements from revisions to IAS 19,

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	rather CEIOPS should consider the appropriateness of a revised IAS 19 as a basis for economic valuations when it is published.