AA Insurance

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24 August 2018

Richard Johnson, Senior Adviser
Prudential Supervision Department
Reserve Bank of New Zealand
PO Box 2498
Wellington 6140

Emailed to: InsuranceLeasesConsultation@rbnz.govt.nz

Dear Richard,

Submission on Consultation Paper: Insurance Solvency Standards and NZ IFRS 16 Leases

This submission is from AA Insurance Limited (AA Insurance), 46 Sale Street, Auckland.

Thank you for the opportunity to provide feedback in relation to Insurance Solvency Standards and NZ IFRS 16 Leases.

About AA Insurance

AA Insurance is a joint venture between Vero Insurance New Zealand Limited (VINZL) and the New Zealand Automobile Association Limited (NZAA) underwriting and selling domestic building, contents and motor policies, and commercial small business and pleasure craft policies (closed to new business). The effective ownership of AAIL is 68% Suncorp (shareholding via Vero NZ) and 32% NZAA.

AA Insurance operates the AA Insurance brand in New Zealand and employs approx. 740 people, writes insurance policies to the value of approximately $390m per annum, and insures approx. 389,000 customers who hold 753,000 policies.

AA Insurance responses to the questions raised in the Consultation Paper are detailed on the following pages. Please let us know if you have any questions or require any further information.

Yours sincerely

M. Chl

Martin Chisholm
Head of Finance

AA Insurance response to the questions raised in the Consultation Paper

Please note that responses are provided from a lessee's perspective as the company does not operate as a lessor.

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Q: Is the description of the accounting approaches discussed in Part 3 consistent with your understanding of the current and new accounting approaches for lease contracts? If not, please provide an explanation of the differences.

A: The description of the accounting approaches is consistent with our understanding.

Q: Are there any requirements of NZ IFRS 16 that you consider the Reserve Bank needs to make specific provision for in the Solvency Standard in addition to or instead of those set out in Part 2?

A: We are not aware of any additional requirements at this stage.

Q: Are there any elements of NZ IFRS 16 transition proposals that you consider the Reserve Bank needs to consider?

A: AA Insurance is in the process of investigating the transition proposals under NZ IFRS 16. We anticipate the impact to actual capital at transition, under the proposal set out in the Consultation Paper, to be immaterial however this is subject to further analysis.

The Solvency Standard requires solvency forecasts to be provided in the annual and half yearly solvency return. As a result, there is a need to determine transitional provisions in respect of the forecast period to provide insurers with certainty of application of NZ IFRS 16 and to allow insurers to prepare the relevant calculations.

We agree with the ICNZ submission that the treatment of leases under NZ IFRS 16 should be adopted in the solvency return forecasts from the first return in which the insurer transitions to NZ IFRS16. For example, an insurer with a June balance date will have the standard become mandatory for the financial year ending 30 June 2020. In this case, it is proposed that the first solvency return to reflect NZ IFRS 16 for both actual and forecast solvency would be the return in respect of the half-year ended 31 December 2019. Prior to this date, the actual and forecast solvency should be based on the existing lease accounting standard.

Q: Are there any other specific lease related transactions that the Reserve Bank should consider from a Solvency Standard perspective?

A: At this stage, we are not aware of any other specific lease related transactions that the Reserve Bank needs to consider.

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Q: Do you consider that the nature of the potential risks of lease contracts and the accounting treatment of NZ IFRS 16 set out in Table 2 are reasonable?

A: We believe the nature of the potential risk of lease contracts and the accounting treatment of NZ IFRS 16 set out in Table 2 are reasonable.

Q: Are there any risks that have been ignored or inappropriately characterised?

A: Based on our current understanding, we do not believe that there are risks that have been ignored or inappropriately characterised.

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Q: Do you consider that the proposed approach appropriately addresses the key risks identified in Table 2? If not, please provide an explanation and recommend an alternative approach.

A: AA Insurance believes that the proposed approach addresses the key risks in Table 2, except in regard to the following matters:

(1) Right-of-use assets which are intangible should be exempted from the full deduction from actual capital that applies to other intangible assets.

(2) The interest rate capital charge was not explicitly discussed in Table 2. Interest rate capital charge should generally not apply to right-of-use assets as these assets are not subject to interest rate movements.

Q: Do you consider that the draft text set out in Appendix B, would effectively implement the proposed changes?

A: We believe the draft text set out in Appendix B will effectively implement the proposed changes subject to the following comments:

(1) New paragraph 28A – remove "where the underlying assets is tangible".

(2) New paragraph 62A – prefer the first option

(3) New paragraph 66A – prefer the first option

Q: Do you have any further points about NZ IFRS 16 Leases you would like to bring to the Reserve Bank's attention?

A: We have no further points to add.

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Q: *If your firm is an overseas licensed insurer under the Insurance (Prudential Supervision) Act, please indicate, if known, how the home regulator has or is expected to respond to the introduction of IFRS 16 for regulatory capital purposes.*

A: Not applicable.

[redacted]

[redacted]

[redacted]