ED 5 Insurance contracts

CL 2

General comments

As an industrial group Holcim is unlikely to be much affected by the resulting IFRS. Neither would we claim to have any deep expertise or practical experience in the area of insurance accounting which would enable us to make a worthwhile contribution to the technical discussion on ED 5. We therefore confine our comments to a few specific areas which are, or could be, relevant for industrial companies.

Nevertheless, we appreciate that there are many difficult technical problems to solve, even in the "stop-gap" *Phase I.* This seems to be the case especially in the area of mismatch of asset and liability measurement bases, for instance. We would therefore encourage the Board to work actively and pragmatically with our fellow preparers in the insurance industry to find appropriate solutions for *Phase I*: for the stop-gap in particular, practicality should be allowed to take precedence over conceptual purity where the two conflict.

ED 5 does not mention the question of consolidation. We believe that this is a gap which could prove problematical for industrial companies which have **captive insurance subsidiaries** and ask you to devote some attention to it. As we see it, ***inter-company*** insurance contracts and their financial effects should be eliminated on consolidation, in line with IAS 27. Furthermore, any "reinsurance" contracts made by a captive insurance subsidiary with a third party to lay off other subsidiaries' risks have rather the economic substance of "insurance" contracts from the consolidated viewpoint ("as if one company"). They should be treated as such in the consolidated financial statements. This would mean that, since the group is a 'net' holder (i.e. a 'net' policyholder), **such reinsurance contracts would in fact fall outside the scope of the proposed IFRS.**

We support the principle that you have adopted in this and other standards that scoping should be based on type of transaction, not on type of industry. However, this does mean that, where a relatively small amount of a given transaction-type occurs in a group, that group has potentially to fulfil many cumbersome, costly requirements (especially, but not only, in disclosures) which are actually primarily only directed towards a particular "industry". For example, an industrial group's captive insurance subsidiary might undertake a minor amount of third-party insurance business, as a small side-line to bring in some extra contribution, and thus put the group in the position of having to set up more complex systems to account for and collect data and to make disproportionate disclosures (e.g. in line with paragraphs 26-30 in ED 5). In IAS this problem was overcome by the *opening materiality clause in a standard*, but in ED 5 as in the IASB's other proposals to date this clause has been dropped, without any practical, pragmatic substitute. We strongly request the IASB to take up the question of describing sensible materiality considerations – for this and for other proposals – as a matter of urgency.

Another gap in ED 5 is any consideration of income statement effects. We understand the IASB's fair value approach of "look after the balance sheet and the income statement will look after itself". However, for preparers and for the majority of grass-root users, it is the income statement which is the key presentation, directed at showing the real, underlying sustainable results of the business both as an indication of what has happened and as a starting-point for forecasting what will happen. For these purposes the balance sheet is of secondary importance. We hope that *Phase II* of the insurance project will consider carefully how the real, underlying sustainable results of insurance business should be presented.

Procedurally, we have doubts about the legitimacy of the Board's approach on measurement. We believe that, at least until the issue of fair value measurement has been subject to a thorough due process, the IASB's proposals can only legitimately be accepted where it would also offer more widely accepted, traditional measurement assumptions - at least as alternatives. Implicitly *ED 5* assumes that *Phase II* will take a fair-value approach and asks for endorsement of the disclosure of fair values from December 2006 onwards without proposing how this is to be arrived at – especially in an area where market values are practically non-existent. Therefore we strongly believe, for the reasons cited above, that such a disclosure should not be mandatory.

Yours sincerely
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