

www.allianz.com

Allianz, 80790 Munich, Germany

International Accounting Standards Board
Sir David Tweedie, Chairman
30 Cannon Street
London EC4M 6XH

United Kingdom

Koeniginstrasse 28
80802 Munich, Germany
Phone +49 89 38 00-0
Fax +49 89 38 00-34 25

Commerzbank AG
Bank code 700 800 00
Account No. 310 922 700
IBAN DE48 7008 0000 0310 9227 00
SWIFT-BIC DRESDEFF700

Direct dial
Tel. +49 89 38 00-14429
Fax +49 89 38 00-8-14429
Mail louise.jordan@allianz.com

Our ref., Date
Louise Jordan
15 March 2011

ED/2010/13, *Hedge Accounting*

Dear Sir David,

We appreciate the opportunity to comment on the IASB's exposure draft 2010/13 – *Hedge Accounting* (the "ED"). As a member of the European Insurance CFO Forum we would like to state that we support the comment letter submitted by the CFO Forum and the Comité Européen des Assurances (CEA) dated 9 March 2011 and thus support the IASB's objective to replace the current hedge accounting requirements as part of their project to replace IAS 39.

We believe the ED is a strong step in the right direction, in particular, we agree that:

- Hedge effectiveness testing is less burdensome as the requirements of retrospective testing as well as the quantitative threshold (80-125%) are removed.
- The proposed standard is more principal based and the documentation requirements are reduced. Thus, entering into hedge relationships will be less burdensome and more often in line with the underlying economics.
- The proposed standard enables an entity to apply hedge accounting in more situations, as the scope of both eligible hedging instruments and eligible hedged items is increased.

We appreciate that the ED's objective is not only based on the link between an entity's risk management and financial reporting but also focuses on the accounting mechanics, such as mitigating an accounting mismatch between derivatives and hedged items. Furthermore, we believe that the objective to align risk management with hedge accounting can not always be achieved as they have different objectives, methodologies and techniques. Moreover, we believe the new hedge accounting rules should in particular emphasize the reduction of accounting mismatches, as explained in the next paragraphs.

Based on the proposed new hedging rules, a situation in which an accounting mismatch may arise is when a reporting entity classifies equities as 'fair value through other comprehensive income' at the acquisition date. In subsequent periods, an entity may decide to hedge its equity risk exposure

via a forward sale contract. From an economic perspective, fair value fluctuations of the equities are offset by fair value changes of the forward sale contract, and thus, the entity is not exposed to equity risk anymore.

However, the ED proposes that hedge accounting cannot be applied to equities classified as 'fair value through other comprehensive income'. Based on the ED, profit and loss volatility may arise as fair value fluctuations of the equities are recognized in other comprehensive income, whereas fair value fluctuations of the forward contract are recognized in profit or loss. In order to avoid such an artificial accounting mismatch, we believe that equities should qualify as hedged items. Such a treatment will be consistent with the IAS 39 hedging rules as they permit equities, classified as available-for-sale, to be designated as hedged item.

As an insurer, we are especially interested to reduce the artificial accounting mismatch that could arise when we hold a portfolio of fixed interest rate assets (such as bonds) at amortized cost and carry insurance liabilities at fulfillment value. Both fixed interest rate assets and insurance liabilities share interest rate risk, that gives rise to opposite changes in fair value that tend to offset each other (assuming duration matches).

The critical issue arises whether interest rate changes give rise to an accounting mismatch between fixed interest rate assets and insurance liabilities. To avoid such an accounting mismatch, we believe the new hedge accounting rules should enable a valid hedge relationship between fixed interest rate assets and insurance liabilities. We believe that this aspect should be covered in the next phase of the project, hedge accounting for open portfolios.

The financial instruments project, including hedge accounting, and the insurance contracts project are interrelated as both projects determine whether and to which extent an accounting mismatch arises between an insurer's assets and liabilities. If the forthcoming standards introduce similar recognition and measurement provisions that correspond to each other they can provide a true and fair view only when applied combined. Therefore, we would like to repeat our comment, stated in the comment letter *Request for Views on Effective Dates and Transition Methods* that the effective dates of IFRS 9 and the future insurance standard should be aligned.

We would be pleased to discuss our comments with you.

Yours sincerely,



Louise Jordan
Vice President, Group Accounting
Accounting Policy Department



Dr. Dietmar Isert
IFRS Specialist, Group Accounting
Accounting Policy Department