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FOR THE ATTENTION OF THE INTERNATIONAL ACCOUNTING STANDARDS BOARD

23 November 2004

COMMENTS ON EXPOSURE DRAFT 7 FINANCIAL INSTRUMENTS: DISCLOSURES BY CEA (COMITÉ EUROPÉEN DES ASSURANCES)

General Comment

The Comité Européen des Assurances (CEA), representing the European insurance and reinsurance sectors, is pleased to comment on Exposure Draft 7 Financial Instruments: Disclosures.

CEA fully supports the principles underpinning the EU-initiated process aiming at a strong, consistent and workable set of accounting standards. Consequently, we are keen to participate actively in the development of the IASB projects.

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Key message

1. We strongly support the overall objective of moving to a principle-based approach for disclosure requirements in relation to financial instruments of any entity. We also support that all disclosures requirements regarding financial instruments should be concentrated in one standard.

2. We suggest that disclosure requirements on sensitivity analysis would be reassessed with the developments of Phase II Insurance Contracts as the inclusions of such risk disclosures at this stage would lead to potential misunderstanding of financial reality and repetitive changes.
   Moreover, we are not convinced that financial statements would be the right place for this type of information. That information should be preferably disclosed in the operating and financial review of the company. However, companies which are willing to publish quantitative sensitivity analysis may do it, but it cannot be made mandatory.

3. We support the proposal that insurance companies should be left to determine how to make the required capital disclosures in ways that best meet the user's requirements and protect the entity's proprietary information.
   However, as the actual insurance solvency requirements are applied inconsistently on a worldwide basis and even across Europe, we are not convinced that the required capital disclosures in the financial statements will enhance comparability and transparency for account users.

4. ED 7 cancels certain requirements of IFRS 4 and other IFRS standards. However, as per IFRS 4 and other IFRS standards, those requirements should be applied in 2005-2006 but cancelled as at 1 January 2007 by ED 7. We believe there is no reason to make them compulsory for 2005-2006, especially as the insurance companies applying ED 7 as from 1 January 2005 will not need to apply those requirements anymore. As a consequence, we propose a new paragraph to set 01 January 2005 as the effective date for the requirements of ED 7 which cancel requirements of IFRS 4 and other IFRS standards.

Here below, we have noted our concerns as to some aspects of the proposed approach and our responses to the specific matters on which comment was requested.

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Question 1 – Disclosures relating to the significance of financial instruments to financial position and performance

The draft IFRS incorporates disclosures at present contained in IAS 32 Financial Instruments: Disclosure and Presentation *so that all disclosures about financial instruments are located in one Standard. It also proposes to add the following disclosure requirements:*

a) financial assets and financial liabilities by classification
b) information about any allowance account
c) income statement amounts by classification
d) fee income and expense.

Are these proposals appropriate? If not, why not, what alternative disclosure would you propose?

We strongly support the overall objective of moving to a principle-based approach for disclosure requirements in relation to financial instruments of any entity. We also support that all disclosure requirements regarding financial instruments should be concentrated in one standard. Therefore, we consider that generally this proposal is appropriate.

Question 2 – Disclosure of fair value of collateral and other credit enhancements

For an entity's exposure to credit risk, the draft IFRS proposes to require disclosure of the fair value of collateral pledged as security and other credit enhancements unless impracticable. Is this proposal appropriate? If not, why not? What, if any, alternative disclosures would you propose to meet the stated objective?

We do not have specific comment on this question.

Question 3 – Disclosure of a sensitivity analysis

For an entity that has exposure to market risk arising from financial instruments, the draft IFRS proposes to require disclosure of a sensitivity analysis. Is the proposed disclosure of a sensitivity analysis practicable for all entities? If not, why not and what, if any, alternative disclosures of market risk would you propose to enable users to evaluate the nature and extent of market risk?

It is clear that the development of sensitivity analysis would represent a significant task for European insurance companies. We are also concerned that this information may not be easily auditable.
As a consequence, the quality of this information could lack the necessary level of reliance for users to evaluate clearly the nature and the level of the risks concerned.
Finally, in order to avoid repetitive changes, we suggest that disclosure requirements on sensitivity analysis could be reassessed with the development of Phase II Insurance Contracts.

Moreover, linked to the auditability, we wonder whether financial statements would be the adequate place for this type of information.

However, companies which are willing to publish quantitative sensitivity analysis may do it, but it cannot be made mandatory.

Question 4 – Capital disclosures

The draft IFRS proposes disclosure of information that enables users of an entity's financial statements to evaluate the nature and extent of its capital. This includes a proposed requirement to disclose qualitative information about the entity's objective, policies and processes for managing capital; quantitative data about what the entity regards as capital; whether during the period it complied with any capital targets set by management and any externally imposed capital requirements; and if it has not complied, the consequences of such non-compliance.
Is this proposal appropriate? If not, why not? Should it be limited to only externally imposed capital requirements? What, if any, alternative disclosures would you propose?

We agree with the proposal that companies should be left to determine how to make the required capital disclosures in ways that best meet the requirements of users and protects the entity's proprietary information.

However, we feel that at this point in time, it is not appropriate for IFRS to require this disclosure in IFRS financial statements for several reasons:

- We do not consider it adequate to require disclosures of internal capital targets because those are commercially sensitive and not necessary relevant for an understanding of the financial statements;
- For the time being, capital requirements are applied inconsistently on a worldwide basis and even across Europe. This issue could lead to difficulties in comparison and analysis for users;
- We do not consider it appropriate to require disclosures on compliance with internal or external capital requirements as we believe financial statements are not the right place for this type of information.

Question 5 – Effective date and transition

The proposed effective date is for periods beginning on or after 1 January 2007 with earlier adoption encouraged. Entities adopting IFRS and the draft IFRS for the first time before 1 January 2006 would be exempt from providing comparative disclosures for the draft IFRS in the first year of adoption. Are the proposed effective date and transition requirements appropriate? If not, why not? What alternative would you propose?

ED 7 cancels certain requirements of IFRS 4 and other IFRS standards. However, as per IFRS 4 and other IFRS standards, those requirements should be applied in 2005-2006 but cancelled as at 1 January 2007 by ED 7. We believe there is no reason to make them compulsory for 2005-2006, especially as the insurance companies applying ED 7 as from 1 January 2005 will not need to apply those requirements anymore.
As a consequence, we propose a new paragraph to set 1 January 2005 as the effective date for the requirements of ED 7 which cancel requirements of IFRS 4 and other IFRS standards.
This paragraph should at least be applied to the following paragraphs: IFRS 4 (39b, IG49 to IG50 except IG 49a, IG49f and IG50f).

Question 6 – Location of disclosure of risks arising from financial instruments

The disclosure of risks arising from financial instruments proposed by the draft IFRS would be part of the financial statements prepared in accordance with International Financial Reporting Standards. Some believe that disclosures about risks should not be part of the financial statements prepared in accordance with IFRS; rather they should be part of the information provided by management outside the financial statements. Do you agree that the disclosures proposed by the draft IFRS should be part of the financial statements? If not, why not?

We think there should be an option to include information on risks in a section on financial risk management in the operating and financial review where this is produced but not necessarily in the financial statements.

Question 7 – Consequential Amendments to IFRS 4

Paragraph B10 of Appendix B proposes amendments to the risk disclosures in IFRS 4 Insurance Contracts *to make them consistent with the requirements proposed in the draft IFRS.*
The requirements in IFRS 4 were based on disclosure requirements in IAS 32 that would be amended by the draft IFRS. Do you agree that the risk disclosures in IFRS 4 should be amended to make them consistent with the requirements proposed in the draft IFRS? If not, why not and what amendments would you make pending the outcome of phase II of the Board's insurance project?

If certain quantitative requirements discussed above remain unchanged in ED 7, insurance companies will be discouraged from applying ED 7 before 1 January 2007. We nevertheless recommend the inclusion of a specific paragraph as explained in our answer to question 5.

Moreover, the financial instruments that companies issue often contain an interest guarantee and a DPF for which measurements have not yet been solved and should not be solved until the Phase II Insurance Contracts finalisation. Before that, it is too early to require presentation of the fair values of the contracts and a sensitivity analysis. It is not reasonable that the outcome of Phase II Insurance Contracts differs from the application of ED 7.

Question 8 – Implementation Guidance

The draft Implementation Guidance accompanying the draft IFRS suggests possible ways to apply the risk disclosure requirements in paragraphs 32 – 45. Is the Implementation Guidance sufficient? If not, what additional guidance would you propose?

Currently, we do not have any specific comments.

Question 9 – Difference from the Exposure Draft of proposed Statement of Financial Accounting Standards *Fair Value Measurements* published by the US Financial Accounting Standards Board.

The FASB's Proposed Statement of Financial Accounting Standards Fair Value Measurements, which is open for public comment at the same time as this Exposure Draft, proposes guidance on how to measure fair value that would apply broadly to financial and non-financial assets and liabilities that are measured at fair value in accordance with other FASB pronouncements. That Exposure Draft proposes disclosure of information about the use of fair value in measuring assets and liabilities as follows:

(a) For assets and liabilities that are remeasured at fair value on a recurring (or ongoing) basis during the period (for example, trading securities)
  - *(i) the fair value amounts at the end of the period, in total and as a percentage of total assets and liabilities,*
  - *(ii) how those fair value amounts were determined (whether based on quoted prices in active markets or on the results of other valuation techniques, indicating the extent to which market inputs were used), and*
  - *(iii) the effect of the remeasurements on earnings for the period (unrealised gains or losses) relating to those assets and liabilities still held at the reporting date.*

(b) For assets and liabilities that are remeasured at fair value on a non-recurring (or periodic) basis during the period (for example, impaired assets), a description of
  - *(i) the reason for remeasurements,*
  - *(ii) the fair value amounts,*
  - *(iii) how those fair value amounts were determined (whether based on quoted prices in active markets or on the results of other valuation techniques, indicating the extent to which market inputs were used), and*
  - *(iv) the effect of the remeasurements on earnings for the period relating to those assets and liabilities still held at the reporting date.*

Disclosures similar to (a)(ii) above are proposed in paragraph 31 of the draft IFRS (and are currently required by paragraph 92 of IAS 32) and disclosures similar to (a)(iii) are proposed in paragraph 21(a).
Do you agree that the requirements in the draft IFRS provide adequate disclosure of fair value compared with those proposed in the FASB's Exposure Draft? If not, why not, and what changes to the draft IFRS would you propose?

Currently, we do not have any specific comments.

Question 10 – Other comments

Do you have any other comments on the draft IFRS, Implementation Guidance and Illustrative Examples?

We have no other comments.