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EFRAG's draft comment letter: ESMA's Consultation Paper on 'ESMA Guidelines on Alternative Performance Measures'

Dear Madam or Sir

As the German Insurance Association (GDV) we appreciate the opportunity to share our views with respect to EFRAG's draft comment letter on the Consultation Paper 'ESMA Guidelines on Alternative Performance Measures' (ESMA/2014/175) published by ESMA on 13 February 2014.

The objective of IFRS financial statements is to provide relevant information about financial position and financial performance of the reporting entity. An appropriate performance reporting is of utmost importance for long-term oriented insurers. In general, we agree with European Securities and Markets Authority (ESMA) that it should be clearly understandable and transparent for investors what the Alternative Performance Measures (APMs) are intended to express (**Question 8**). Nevertheless, we mostly share the concerns expressed by EFRAG in its draft comment letter. The change in APMs' definition, an extended scope of the [draft] ESMA Guidelines and the additional excessive disclosure requirements as a result of the 'complain or explain' approach would lead to significantly increased work overload for issuers. For these reasons we suggest keeping the current definition of an APM (paragraph 10 of EFRAG's draft comment letter). Furthermore, we support the EFRAG's view regarding its objections against inclusion of prospectuses and related documents into the scope of the ESMA Guidelines (paragraph 13 of EFRAG's draft comment letter).

We believe however that it is very important that the final comment letter of EFRAG provides more specific rational why the [draft] ESMA Guidelines are too extensive and do not entirely pass the cost-benefit-test via answering some specific questions of ESMA's Consultation Paper. In particular, we strongly encourage EFRAG to heavily oppose the impractical and overly burdensome requirement to accompany in general the use of any APM with reconciliations to amounts presented in the financial statements (**Question 7**). Especially, the requirement to separately explain the

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'each reconciling item' (paragraph 22 of the [draft] ESMA Guidelines) would lead to excessive disclosure requirements. We recommend EFRAG to explicitly request the removal of paragraphs 22 - 25 of the [draft] Guidelines without replacement. From the insurers' perspective there is at present no common base to produce such reconciliations as the final standard IFRS 4 *Insurance Contracts* (Phase II) is not available yet. Thus, the objective to increase the understandability and comparability of financial information of insurers can't be achieved without undue costs for issuers before the final high-quality standard becomes effective (**Question 13 & Question 14**). Indeed, one of the main reasons for use of APMs by insurers (e.g. embedded value) might be the matter of fact that the key IFRS for insurers is unfortunately still under development.

Furthermore, the GDV has the firm view that the [draft] ESMA Guidelines might have the unintended consequence being contradicting the efforts undertaken by the IASB's Disclosure Initiative which aims to reduce the information overload and to improve the disclosure of financial statements. In addition, IAS 1 *Presentation of Financial Statements* allows entities the flexibility to provide business model & entity specific information. Thus, although we share the rational for the existing CESR Recommendation on Alternative Performance Measures (October 2005), the requirements of the [draft] ESMA Guidelines go far beyond the initial rational and will lead unavoidable to overload of additional financial disclosures. We fully share concerns as expressed in paragraph 23 of EFRAG's draft comment letter.

Finally, we do not fully understand the interaction between the expectations of ESMA regarding the actions the national competent authorities (NCAs) should take and expectations regarding the issuers themselves before the NCA undertakes an action. We encourage EFRAG to advocate for an explicit change that issuers themselves are not affected by the final ESMA Guidelines directly. The NCAs should decide how to implement the ESMA Guidelines /or not if unnecessary/ considering the issuers behavior.

We hope that our comments will be helpful to TEG's members in reaching their final conclusions on the ESMA's Consultation Paper. If you would like to discuss our comments further, we would be very delighted.

Yours sincerely,

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Annex

Q1: Do you agree that the ESMA [draft] guidelines should apply to all issuers defined as a legal entity governed by private or public law, other than Member States or Member State's regional or local authorities, whose securities are admitted to trading on a regulated market, the issuer being, in the case of depository receipts representing securities, the issuer of the securities represented regardless of the financial reporting framework they use to report? If not, why?

No, irrespective of the comparability argument, we do not consider it fully appropriate to include entities which are not applying the International Financial Reporting Standards (IFRS) but still being issuers into the scope of the [draft] ESMA Guidelines. Especially, in such cases the initial rational for the issuance of the Guidelines on the use of APMs by CESR [Ref: CESR/05-178b, October 2005] does not apply, as the formats for balance sheet and income statement are prescribed by the Accounting Directive 2013/34/EU. In particular, we remind that the initial CESR Recommendation referred to the decision of the European Commission that the formats laid down in the European Accounting Directive do not apply to IFRS [consolidated] financial statements. We encourage EFRAG to consider the inclusion of this aspect into its final comment letter.

Q4: Do you believe that issuing ESMA guidelines constitute a useful tool for dealing with the issues encountered with the use of APMs? If not, why?

If designed in an appropriate way the ESMA Guidelines might constitute a useful tool for dealing with variety of ways on which issuers are communicating its financial position or performance to users when using flexibility of IAS 1 *Presentation of Financial Statements*. Nevertheless, we have the strong view that solely the International Accounting Standards Board (IASB) should remain responsible to design disclosure requirements for financial reporting purposes. Especially, we note that the IFRS requirements are developed by the IASB already with the primarily objective to meet the expectation of investors and other users of financial statements on the capital markets.

Furthermore, we do not fully understand the interaction between the expectations regarding the actions the national competent authorities (NCAs) should take and expectations regarding the issuers themselves before the NCAs undertake an action. We are concerned about the potential consequences regarding if and to whom the issuers should report if they do not complain with the ESMA Guidelines, and especially when it is the case. Should every European NCA create a register of issuers who are non-compliant and oblige the entities to report? We would strongly disagree with such a bureaucratic approach if intended by ESMA. Thus, we do kindly recommend EFRAG to explicitly advocate for an explicit change that issuers themselves are not affected by the ESMA Guidelines directly. The NCAs should decide how to implement the ESMA Guidelines /or not if unnecessary/ considering the issuers behavior in national markets.

Q7: Do you agree that issuers should disclose a reconciliation of an APM to the most relevant amount presented in the financial statements? If not, why?

The GDV does not share the view of ESMA [draft] Guidelines that the reporting of all quantitative information not defined by the applicable financial reporting framework should result in additional, in our view excessive, disclosure requirements. In particular, because we note that ESMA [draft] Guidelines suggest that any numerical measure (...) not defined under IFRS would be considered as an APM (paragraph 15 of the [draft] ESMA Guidelines).

The GDV does not agree that issuers should in general disclose a reconciliation of an APM. We have the strong view that this requirement would be overly burdensome to issuers without any significant benefit to users. It would rather unavoidable lead to information overload. Furthermore, it would contradict the objective of the IASB's Disclosure Initiative which aims to ensure a level of effective disclosure requirements.

We strongly believe that the requirement to explain the objective of a particular APM is suitable and sufficient enough to achieve an understandable information flow between issuers and users. For example, it is from our perspective appropriate to provide a clear and understandable rational, what the Embedded Value as an APM is intended to express. But it is not appropriate and fully unnecessary to requite the detailed reconciliation of Embedded Value to the numbers in financial accounts.

Finally, it is unclear to us how the reconciliation of a particular APM should be exercised when the particular APM is used between the reporting dates (e.g. in a press release on 31 May). Should the reconciliation refer to numbers in the interim report of 31 March or to the forecast of numbers of 30 June?

For the reasons above we strongly request the removal of paragraphs 22 - 25 of the [draft] Guidelines without replacement.

Q10: Do you agree that issuers should explain the reasons for changing the definition and/or calculation of an APM? If not, why?

Q11: Do you believe that issuers should provide comparatives and/or restatements when an APM changes? If not, why?

We support the view that particular APM should be used in a consistent and understandable way over time.

However, having the strong view that reconciliations of APMs should not be required by the final ESMA Guidelines we consequently believe that also the requirement in the paragraph 31 of the [draft] ESMA Guidelines) should be removed.

Consequently, we suggest deleting the paragraph 31 of the [draft] ESMA Guidelines without replacement.

Q12: Do you believe that issuers should provide explanations when they no longer use an APM? If not, why?

Regarding the requirements on consistency in paragraph 34 of the [draft] ESMA Guidelines we suggest to delete the words "*or no longer use*". We believe that consistency argument does not apply if an issuer decided to no longer use a specific APM. As the use of a particular APM is not required, the issuer should not be obliged to explicitly justify why the use of a particular APM is considered to be not necessary by the management. Especially, there is no danger of misleading information for investor decisions if the specific APM is not used any more.

Consequently, we suggest deleting the paragraph 38 of the [draft] ESMA Guidelines without replacement.

Q13: Do you agree that the [draft] guidelines will improve transparency, neutrality and comparability on financial performance measures to users? If not, please provide suggestions.

We believe that the transparency of financial communication is in danger when the final ESMA Guidelines would remain containing the reconciliation requirements. And the comparability with regard to reconciliation can't be achieved as long as the common starting base (IFRS 4 *Insurance Contracts* Phase II) is not available.

Thus, we strongly suggest deleting the paragraphs 22 - 25 of the [draft] ESMA Guidelines without replacement.

Q14: Do you agree with the analysis of the cost and benefit impact of the [draft] guidelines? Please provide any evidence or data that would further inform the analysis of the likely cost and benefits impacts of the proposals.

The GDV does not agree with the cost/benefit analysis in the ESMA Consultation Paper. We do believe that especially the costs for users are not sufficiently weighted. Nowadays users are already expressing their concerns about information overload. The IASB is recently trying to address these valid concerns via the 'Disclosure Initiative' which we support. Also preparers of financial statements like insurers express continually the serious concerns regarding the positive cost/benefits relation regarding the IFRS disclosure requirements.

We are afraid that [draft] ESMA Guidelines on the use of APMs might have the unintended consequence that the efforts of IASB would be contradicted as not reduction but additional detailed information as suggested by the Consultation Paper would be required. In our view, the right approach would be to ensure that only the relevant disclosures are transparently provided. The techniques how the APMs are calculated are highly different and in many cases quite sophisticated (e.g. Embedded Value calculations). The sufficient objective of ESMA Guidelines should be to ensure that clear and understandable explanation is provided what a particular APM is meant to express. This should be encouraged or even required as a sufficient measure. For these reasons ESMA should redesign the Guidelines to focus them on how to ensure the usefulness and effectiveness of the financial information provided to users.