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Mrs Françoise Flores
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Email: commentletters@efrag.org

October 25, 2013

Re: Draft comment letter EFRAG on IASB ED Insurance Contracts

Dear Mrs Flores,

The Fédération Française des Sociétés d'Assurances (FFSA) welcomes the opportunity to comment on EFRAG's draft comment letter on the IASB Exposure Draft ED/2013/7: Insurance Contracts. Our members represent most of the French insurance and reinsurance undertakings, constituting over 90% of the insurance market in France. Accordingly it represents the consensus view of a significant element of the European insurance industry.

1. We agree with EFRAG that the IASB has made positive steps in considering the requests of the stakeholders. We support the IASB decisions regarding the adjustment of the contractual service margin (CSM) for changes in estimates of expected cash flows related to future coverage and other future services. We also welcome the introduction of other comprehensive income (OCI) for changes in market interest rates on insurance liabilities, the top down approach for discount rate and the revised transition proposals.
2. We agree with EFRAG that the accounting requirements for insurance liabilities should not ignore the interactions between the insurance liabilities and their backing assets. The insurance liabilities' profile drives the portfolio of related investments. Insurance liabilities are to a large extent long-term and predictable, with stable cash-flow profiles. As consistently expressed in our comment letters to the 2010 ED and IFRS 9, the interaction between insurance liabilities and their backing assets is the core of the insurance activity and its performance, and is illustrated through the asset liability management (ALM) strategies. A consistent measurement of the insurance liabilities and their backing assets is fundamental to reflect their overall linkage.

We agree with EFRAG that the IASB should acknowledge the existence of this long-term investment “liability-driven” business model. In this respect, the re-introduction of a FV-OCI¹ measurement in IFRS 9 and the requirement to present in OCI the changes in market interest rates on insurance liabilities that reverse over time as proposed by the IASB are a very positive step. However, like EFRAG, we believe that the FV-OCI measurement category is too restrictive and as such would not permit to reflect the performance of the ALM strategies. We consider that the FVOCI measurement category should be expanded to all categories of assets backing insurance liabilities, including portfolios of derivatives so as to faithfully represent the performance of insurance activities.

3. An appropriate accounting standard for insurers should reflect the long term nature of insurance activities in the P&L. The impact of short-term market fluctuations that reverse over time should not obscure the long-term operating performance of insurance activities. The ED fails to meet this objective particularly with regard to participating contracts. It should be revised to ensure that the performance of all insurance contracts is appropriately reflected in the financial statements. The ED’s proposals result in an inappropriate measurement of participating contracts as they do not reflect the economics of these products nor their performance. To address these concerns, we support the development of an alternative approach for these contracts, based on a consistent set of principles.

Like EFRAG, we support the principle of reflecting the asset dependency in measuring the participating contracts fulfilment cash flows. We share the same concerns than EFRAG on the ED’s proposals for participating contracts. However, our concerns are much greater than those expressed by EFRAG. In this respect, we do not agree with EFRAG in paragraph 43 that “the IASB’s underlying reasoning to propose such a split [to distinguish between different sets of cash flows for measurement purposes] in order to eliminate accounting mismatches to the maximum extent possible and perform the split in a way that matches the economic features of the insurance liability with the economic features of the underlying items” is appropriate. We believe that these proposals contradict the ED’s key principle to measure the insurance contract as a bundle of rights and obligations. It is also not consistent with how participating contracts are managed operationally. As a result, financial information provided to users will neither reflect the economics of the participating contracts nor their performance.

Therefore, we consider that the ED’s proposals for participating contracts are not acceptable and should be revised.

To address these concerns and to ensure an effective accounting treatment of all participating contracts, we support the following set of principles that should be considered comprehensively:

- The measurement model for all participating contracts should be consistent with the general principles of the ED that apply to other contracts under the building blocks approach;
- Participating contracts should be measured at current fulfilment value on the face of the balance sheet without bifurcation of cash flows;
- Asset dependency should be reflected through the use of a discount rate that is derived from the assets to recognise the effect of the unwinding the insurance liabilities in the P&L. Consistently with the general principles of the ED, the difference between the interest rate expense calculated at this rate and the effect of unwinding the insurance liabilities at a current discount rate should be recognised in OCI;

¹ “Fair value through OCI” or “FVOCI” means fair value measurement in the balance sheet with unrealised gains reported in OCI for assets; and current fulfilment measurement in the balance sheet with changes in discount rate reported in OCI for insurance liabilities.

- The CSM of participating contracts should always represent the unearned profit associated with these contracts. It should be determined on a fully unlocked basis, including the changes in assets returns that impact the insurer's share in expected profits. In other words, the CSM should be adjusted for differences in the cash flows due to changes in financial assumptions, except for short term fluctuations that reverse over time. These short term fluctuations, including those that affect the time value of options and guarantees, should be recognised in OCI.

An approach that combines these key principles would respond to our main concerns with regard to participating contracts. It will result in relevant performance in the P&L and reflect the long-term nature of insurance activities as:

- It will distinguish between earned profit that would be recognised in the P&L as services are provided to the policyholders and changes in future expected profits that would be recognised against the CSM;
- Short-term fluctuations that reverse over time, including those that affect the time value of options and guarantees, would be presented in OCI. Presenting in OCI the impact of market rate changes on the time value of options and guarantees is appropriate because those changes are not representative of the current or future performance of the insurer, they are not part of the service to the policyholders and they are expected to reverse over time.

This set of principles is consistent with that used by the European insurance industry to develop an "industry alternative proposal" for participating contracts. We are in the process of assessing its application to our participating products. Sufficient time is needed for this testing to ensure that the application mechanisms work appropriately for various products under different economic scenarios.

4. We believe that further changes are needed to ensure that the unlocking principle is applied consistently to all contracts. Like EFRAG, we welcome the unlocking of the contractual margin as proposed in the ED. We also agree with EFRAG that the CMS should be adjusted for changes in the risk adjustment that relates to future coverage and other services.

However, we consider that further changes to the ED's proposals are needed to ensure that the unearned profits of the insurance contracts are consistently reflected at initial recognition and at subsequent measurement:

- The unit of account used for the release of the CSM should be the portfolio. It would be consistent with how insurers manage their contracts and with the unit of account used for the initial measurement of the CSM;
 - The favorable changes in expected profit after the CSM has been exhausted should lead to rebuilding the CMS only when all prior losses that have been recognized in the P&L are reversed;
 - The CSM should be released over both the period of coverage and the settlement period as the insurer continues to provide services to the policyholders after the end of the coverage period. For accounting purposes, considering that no services are provided to the policyholders after the end of the coverage period neither reflect the economics of the insurance contracts nor the obligations of the insurer towards the policyholders.
5. The ED's proposals for the presentation of revenue and expenses for life insurance activities will not provide useful information to users. In our view, the summarised margin approach that was proposed in the 2010 ED, together with volume information in the notes, will better achieve this objective.

6. Sufficient time should be given to constituents, particularly insurers, to assess the revised proposals of the IASB through extensive testing prior to their finalisation. As stated above, we have significant concerns with some of the ED's proposals. We believe that these ED's proposals should be revised to ensure that appropriate financial information is provided to users. We acknowledge that these changes are significant. However, such changes are necessary to produce final standards that are workable and relevant for the insurance activities. Therefore, it is crucial that the IASB takes sufficient time to revisit its proposals. Similarly, it will be necessary for constituents, particularly insurers, to gain a comprehensive understanding of the revised proposals through their extensive testing. In order to facilitate this testing there should be a review draft setting out the revised proposals. The objective of this extensive testing will be to ensure that these revised proposals do not have unintended consequences and are workable operationally prior to their finalisation.
7. The mandatory effective date of IFRS 9 must be aligned with IFRS 4 for insurers. We consider that insurers should not be required (but permitted) to adopt IFRS 9 before the mandatory effective date of IFRS 4. If the effective dates were not aligned and insurers were required to adopt IFRS 9 in advance of IFRS 4, it would be critical to include sufficient provisions in IFRS 4 to permit insurers to fully reconsider designations and classifications of their financial assets when adopting IFRS 4.

Appendices to this letter

In Appendix 1 we have provided our comments on the questions you have raised in your Appendix 1 "EFRAG's responses to the questions raised in the exposure draft", your Appendix 2 "Additional Comments" and in your Appendix 4 "Suggestions for clarification in the drafting".

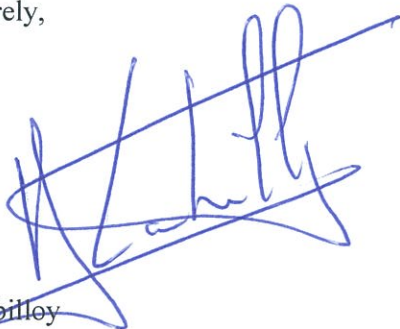
Concerning the field-testing activities, although the FFSA itself has not taken part in EFRAG's field-testing activities, a number of our members have taken part and have provided their feedback separately to EFRAG. Please refer to our above comments on the need of extensive testing after the IASB's proposals have been revised.

In Appendix 2 we have provided you with a copy of our comment letter to the IASB.

We encourage EFRAG to pursue its active dialogue with the insurance industry and with the IASB with the objective of producing high quality IFRSs for both financial instruments and insurance contracts that allow insurers to reflect their business models so as to provide decision-useful information to users.

Please feel free to contact me at +33 1 42 47 93 58 to discuss any matters raised in this letter.

Yours sincerely,



Bertrand Labilloy

Director Economic and Financial Affairs

Appendix 1

Please find hereafter, our comments on the questions you have raised in your Appendix 1 “EFRAG’s responses to the questions raised in the exposure draft”, your Appendix 2 “Additional Comments” and in our Appendix 4 “Suggestions for clarification in the drafting”.

Responses on the additional questions raised in Appendix 1 “EFRAG’s responses to the questions raised in the exposure draft”

▪ *Paragraph 14*

We welcome the decision of the IASB to unlock the CSM for changes in estimates of expected cash flows related to future coverage and other future services. We also agree with EFRAG that the CMS should be adjusted for changes in the risk adjustment that relates to future coverage and other services.

However, we consider that further changes to the ED’s proposals are needed to ensure that the unearned profits of the insurance contracts are consistently reflected at initial recognition and at subsequent measurement:

- The unit of account used for the release of the CSM should be the portfolio. It would be consistent with how insurers manage their contracts and with the unit of account used for the initial measurement of the CSM;
- The favorable changes in expected profit after the CSM has been exhausted should lead to rebuilding the CMS only when all prior losses that have been recognized in the P&L are reversed;
- The CSM should be released over both the period of coverage and the settlement period as the insurer continues to provide services to the policyholders after the end of the coverage period. For accounting purposes, considering that no services are provided to the policyholders after the end of the coverage period neither reflect the economics of the insurance contracts nor the obligations of the insurer towards the policyholders.

We believe the distinction between changes in estimates for future coverage and other services can be made operational without excessive costs. We also think that the future standard should remain principles-based and would object to any further prescriptive guidance being included.

▪ *Paragraph 56*

We consider that an approach that combines these key principles set out in point (3) of our cover letter to EFRAG would respond to our main concerns with regard to participating contracts. This set of principles is consistent with that used by the European insurance industry to develop an “industry alternative proposal” for participating contracts. We are in the process of assessing its application to our participating products. Sufficient time is needed for this testing to ensure that the application mechanisms work appropriately for various products under different economic scenarios.

▪ *Paragraph 57*

We consider that the CSM of participating contracts should always represent the unearned profit associated with these contracts. It should be determined on a fully unlocked basis, including the changes in assets returns that impact the insurer’s share in expected profits. When a contract requires that the amounts paid to policyholders vary with the returns on underlying items, the profit that results from the insurance contract cannot be considered in isolation from those returns. Changes in the expected returns modify the insurer expected profit according to the terms of the contract. If the CSM is not adjusted for these changes, the CSM will not reflect the whole of the unearned profit arising from these contracts and will fail to represent their economics.

In other words, the CSM should be adjusted for differences in the cash flows due to changes in financial assumptions, except for short term fluctuations that reverse over time. Short-term fluctuations that reverse over time, including those that affect the time value of options and guarantees, would be presented in OCI. Presenting in OCI the impact of market rate changes on the time value of options and guarantees is appropriate because those changes are not representative of the current or future performance of the insurer, they are not part of the service to the policyholders and they are expected to reverse over time.

- *Paragraph 58 & 59*

Please refer to point (3) in our cover letter to EFRAG.

- *Paragraph 60*

Yes, we consider that an approach that combines these key principles set out in point (3) of our cover letter to EFRAG would be less complex than the IASB's mirroring approach. For example, it has no requirement to bifurcate cash flows and also benefits from applying the general building block model to these contracts. In addition, it has the advantage to be applicable to all participating contracts with no arbitrary distinction based on an explicit requirement to hold the underlying items.

- *Paragraph 61*

Yes, we consider that an approach that combines these key principles set out in point (3) of our cover letter to EFRAG would result in relevant performance in the P&L. It will also reflect the long-term nature of insurance activities. As such, it would be conducive to useful information for users.

- *Paragraph 87 & 88*

The requirement to disaggregate 'non-distinct' investment components for the P&L presentation is contradictory with the ED principle to separate only those elements of insurance contracts that are distinct. This requirement is complex to implement as it would imply to separate interrelated cash flows and arbitrarily allocate them between the different "components". The data required to disaggregate the investment components is neither readily available nor easy to obtain. It will be unduly costly to obtain. Therefore, we object to this requirement.

- *Paragraph 89*

The ED's proposals for the presentation of revenue and expenses for life insurance activities will not provide useful information to users. In our view, the summarised margin approach that was proposed in the 2010 ED, together with volume information in the notes, will better achieve this objective.

The earned premium revenue as set out in the ED is not an appropriate measure for life insurance business. We are also convinced that insurance analysts and other users of financial statements will neither understand nor rely upon such a presentation. Users will continue to request existing volume measures such as gross written premiums and new business premiums which are key performance indicators for the life insurance industry today.

We consider that these proposals will introduce undue complexity and result in significant implementation costs for insurers without providing any additional benefits to users.

The summarized margin approach, as proposed in the 2010 ED, coupled with the disclosure of volume information in the notes (similar to the volume information that is provided today to users) will better achieve the objective of providing meaningful information to users for life insurance activities. We urge the IASB to reconsider its decision to abandon the summarized margin presentation.

- *Paragraph 103 & 104*

We support the application of the OCI approach for changes in interest rates proposed in the ED. We do not support the approach described in paragraph 103 as envisaged by some, including IASB Board member Stephen Cooper. For participating contracts, please refer to point (3) of the cover letter to EFRAG.

▪ *Paragraph 108 to paragraph 112*

We agree with EFRAG that the accounting requirements applicable to entities should not ignore the interactions between the insurance liabilities and their backing assets. The insurance liabilities' profile drives the portfolio of related investments. Insurance liabilities are to a large extent long-term and predictable, with stable cash-flow profiles. As consistently expressed in our comment letters to the 2010 ED and IFRS 9, the interaction between insurance liabilities and their backing assets is the core of the insurance activity and its performance, and is illustrated through the asset liability management (ALM) strategies. A consistent measurement of the insurance liabilities and their backing assets is fundamental to reflect their overall linkage.

We agree with EFRAG that the IASB should acknowledge the existence of this long-term investment "liability-driven" business model. In this respect, the re-introduction of a FV-OCI measurement in IFRS 9 and the requirement to present in OCI the changes in market interest rates on insurance liabilities that reverse over time as proposed by the IASB are a very positive step.

However, in the IASB general model, financial assets and insurance liabilities are still considered in too much in isolation and are not measured on a consistent basis, irrespective of the ALM strategies. Limiting the FV-OCI measurement category as proposed in IFRS 9 to only simple debt instruments is too restrictive. It would impede insurers to reflect the performance of their ALM strategies and would not faithfully represent the entity's financial performance and performance for contracts.

Therefore, like EFRAG, we believe that the use of FV-OCI should cover all assets involved in the ALM when it aims at matching stable liabilities and would therefore include debt instruments that do not meet the contractual cash flow characteristics, equity shares and property.

However, these ALM strategies are not limited to investment in these assets but involve also portfolios of derivatives hedging, for example, interest rate risks or credit exposures. Therefore, we consider that the FVOCI measurement category should be expanded to all categories of assets backing insurance liabilities, including portfolios of derivatives. It would reflect the performance of our ALM strategies and faithfully represent the performance of insurance activities.

▪ *Paragraph 113*

We acknowledge that expanding the scope of assets measured at FV-OCI raises the issue of impairment, particularly for equity instruments. In this regard, as stated in our comment letter to the ED Financial Instruments: Classification and Measurement, dated 10 September 2009, we recommend that the IASB develop an impairment model for equity instruments that would take into account the investor's holding horizon. We believe that taking into consideration this characteristic would ensure that the business model of long term investors, in particular insurers, is appropriately reflected in the financial statements avoiding undue short term volatility of the markets. Reversal of impairment should also be allowed if there is evidence that the reason for it do not longer exist.

▪ *Paragraph 114*

We do not see any problems in recycling realized gains and loss on investments related to contracts with asset-dependent cash flows. The set of principles that we support for the treatment of participating contracts would appropriately deal with this issue for all contracts with asset-dependent cash flows.

▪ *Paragraph 115*

For those options and guarantees that are not separated according to the requirements of the ED, the recognition of changes in their current value through P&L is not appropriate. It would result in recognising in the P&L short-term market fluctuations that are not representative of the long-term operating performance of the insurer. These short term fluctuations, including those that affect the time value of options and guarantees, should be recognised in OCI.

It will result in relevant performance in the P&L and reflect the long-term nature of insurance activities as:

- It will distinguish between earned profit that would be recognised in the P&L as services are provided to the policyholders and changes in future expected profits that would be recognised against the CSM;
- Short-term fluctuations that reverse over time, including those that affect the time value of options and guarantees, would be presented in OCI. Presenting in OCI the impact of market rate changes on the time value of options and guarantees is appropriate because those changes are not representative of the current or future performance of the insurer, they are not part of the service to the policyholders and they are expected to reverse over time.

▪ *Paragraph 135*

We consider that insurers should not be required, but be permitted, to adopt IFRS 9 (as a whole) before the mandatory effective date of IFRS 4. This belief encompasses all aspects of IFRS 9, including the impairment proposals.

▪ *Paragraph 136*

Yes, for example for investment properties.

Comments on EFRAG's Appendix 2 "Additional Comments"

Disclosure of confidence level

Like EFRAG, we do not agree with this requirement as it will not provide useful information to users. In addition, it would be burdensome to apply. We believe that adequate disclosures on the methodologies and assumptions used to determine the risk adjustment will provide useful information to users and achieve the IASB's objective of transparency.

Gains and losses on buying reinsurance

▪ *Paragraph 17*

For the cedant, the function of reinsurance is to mitigate losses resulting from insurance contracts. Therefore, from an economic perspective, both contracts are linked. Depending on the type of reinsurance contracts, the extent of the mitigation of risk varies. Anyway, the cedant is no more subject to the risks covered under the reinsurance contract.

We are not convinced that the outcome of the ED's proposals appropriately portrays the economics of these transactions in all cases. We recommend that the IASB reassesses the impact of the link between the underlying insurance contracts and the reinsurance contract held on the treatment of the CSM to avoid any unintended or counterintuitive effects of the ED's proposals.

Disclosures of minimum capital requirements

▪ *Paragraph 23*

We agree with EFRAG's recommendation to delete in the final standard the requirement to disclose information regarding the regulatory framework in which entities operate. Regulatory capital is not part of the financial statements of an entity.

Comments on EFRAG's Appendix 4 "Suggestions for clarification in the drafting"

In our response letter to the IASB we have raised a number of significant issues with the underlying principles in the ED which need to be addressed. We believe focus should be given first to developing appropriate revised proposals. We have therefore not commented on EFRAG's suggestions for clarification in the drafting at this stage. However, we raised some comments on the wording and application guidance in our comment letter to the IASB. Please refer to our response to Question 7 and to our appendix in our IASB comment letter.

Appendix 2 – FFSA comment letter on IASB ED Insurance Contracts

See separate file