CEA
Insurers of Europe

Ms Françoise Flores
Chairman
EFRAG
35 Square de Meeûs
B-1000 Brussels

Ref: Measurement of Liabilities in IAS 37

Brussels, 7 May 2010

Dear Ms Flores,

In response to your draft comment letter on the IASB Exposure Draft on measurement of liabilities in IAS 37, please find enclosed a copy of the CEA comment letter to the IASB.

In this letter we highlight some of our concerns regarding the IASB proposals which we hope will be helpful in finalising EFRAG's comment letter.

Do not hesitate to contact us for any further information.

Yours sincerely,

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To: Sir David Tweedie
Chairman
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Ref: ECO-ACC-10-053

Subject: Measurement of Liabilities in IAS 37

Brussels, 12 April 2010

Dear Sir David,

The CEA is the European Federation of insurers and reinsurers, who represents all types of insurance and reinsurance undertakings, accounting for approximately 94% of total European premium income.

In this letter, we first raise some specific points regarding the proposals contained in the Exposure Draft (the 'ED'). Then we highlight some thoughts on the possible convergence or alignment of the models currently proposed for measurement of 'IAS 37' liabilities and insurance liabilities.

Specific comments on the ED

The ED (in the Appendix B, paragraph 4) explicitly states that '*Even if there is there is evidence to support many outcomes, it is not always necessary to consider distribution of literally all possible outcomes using complex models and techniques. Rather, a limited number of discrete outcomes and probabilities can often provide a reasonable estimate (…)*'. We do support this clarification and share the IASB view on this matter.

However, there are also several areas in the ED which raises concerns in our view. Firstly, the ED requires that for a service obligation, preparers should either use the price that the entity estimates a contractor would charge at a future date to undertake the service (if there is a market for such a service) or preparers should estimate the price it would charge another company to undertake such a service (in case no market exist), including the margin that it would require.

We believe this proposal raises several concerns. If the preparer does intend to fulfil the service obligation it-self in the future, it will be forced to book some future profits (the service margin) inside of the liability. This amount will not turn out to be a cash out flow. When the company releases this margin, it will recognise profits while there will be no increase in its economic situation. Moreover, the profit recognition of the preparer will be counter-intuitive as it will end up recognising profits in the future periods for fulfilling a liability it has caused in the past. We believe that such a margin should not be included in the liability as it will not provide helpful information to users on future cash flows of the company. In addition, we believe that the requirement to use a third party price for service obligations is contrary to the 'lower of fulfilment, transfer and cancelation value' principle (see below) underpinning the model proposed in the ED.

Secondly, the ED states that IAS 37 liabilities should be valued as the *amount that the entity would rationally pay at the end of the reporting period to be relieved from the obligation. Normally, this amount would be the present value of the resources required to fulfil the obligation*. However, the ED requires that in some circumstances, there might is evidence that the entity could cancel the liability or transfer it to

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a third party for a lower amount, then would measure the liability at this lower amount. In principle, we agree with this requirement. However, we believe that in some circumstances, a company may have an interest in keeping the liability on its balance sheet even if it could settle or transfer it for a lower amount. It could be the case for example if the company wants to keep the relationship with a customer, or wants to avoid sharing specific information with third parties. Therefore, we believe that the final standard should clarify that the 'lower of' criteria should be applied only when the company has the intention to transfer or cancel the liability. In addition, we are concerned about the burden of proof of this requirement. We do not believe that the Board's intention is to require companies to perform extensive due diligences to asses all the possible transfer prices with all possible counterparties and encourage the Board to precise this point in the final standard.

Thirdly with regard to onerous contracts arising from transactions within the scope of IFRS 4, we would like to scope them out of IAS 37 as all other contracts within the scope of IFRS 4 are scoped out too.

Finally, we question the rationale for prohibiting companies to take into consideration future change in legislation that would change or discharge the present obligation. Reflecting those changes in the financial statements would provide more accurate information about future cash flows of the company.

Similarities between IAS 37 and insurance contracts models

We note that there are several similarities in the model proposed in this ED and the one being currently developed for insurance contracts. Namely, both models are based on a building block approach including a best estimate, a risk adjustment and discounting. We understand that one of the objectives of the Board is to be consistent across projects when necessary. We believe that, by essence, there are significant differences between an insurance contract and an 'IAS 37' type of contract that may justify differences in some areas.

An insurance liability is the consequence of a contract signed with a customer. The contract requires the payment of a premium from the policyholder in exchange of the insurance cover. In the model currently proposed by the IASB, the day one difference (between the value of the insurance liability and the premium) that may occur generates an additional building block, which does not exist in IAS 37. As a consequence of the contract, the insurance company has some cash in (premiums) and cash out flows (benefits), the balance of which will generate some profit. In the case of an IAS 37 liability, there is no cash inflow and hence, no economic profit can emerge.

Therefore, we believe that the Board should restrain alignment between the two models to the sections which are similar, allowing for differences where adequate.

We look forward to discussing this matter further with you should you have any questions,

Yours sincerely,

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