FÉDÉRATION FRANÇAISE DES SOCIÉTÉS D'ASSURANCES
26, Bd HAUSSMANN, 75311 PARIS CEDEX 09 - TÉLÉPHONE 01 42 47 90 00
TÉLÉCOPIE : 01 42 47 93 11 - http:/www.ffsa.fr/

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

E-mail: Commentletters@efrag.org

Paris, 2 June 2014

Dear Ms Flores,

FFSA comments on the EFRAG research paper: "The role of the Business Model in Financial Statements"

The Fédération Française des Sociétés d'Assurances (FFSA) is pleased to comment on the research paper (RP) *The Role of the Business Model in Financial Statements* issued by the European Financial Reporting Advisory Group (EFRAG), the French Autorité des Normes Comptables (ANC) and the UK Financial Reporting Council (FRC).

We welcome the EFRAG's initiative of issuing this RP on the use of the business model in financial statements.

We support the views expressed in the RP that the business model should play a role in financial reporting. However, we believe that the business model should not only play "a" role but that it should be used as a basis for developing accounting standards. We have long held this view, notably in our responses to the IASB's consultations on financial instruments and insurance contracts projects or to the European Commission's Green Paper on Long Term financing of the European Economy.

Performance of entities results from their activities, e.g. from their business model (or models – entities may have more than one business model). Providing only information on changes in value of assets and liabilities without portraying how the entity uses its assets and liabilities in line with its business models does not result in decision useful information. In such a case, investors are not in a position to assess the "real economic" performance of these entities and the differences between entities with similar business models are obscured.

As such, it is essential that the accounting framework is designed to capture the different business models of entities and reflect them so as to allow an assessment of the economic performance of the entities and of their management's accountability (or stewardship). Where financial statements provide information that is not in line with the business models of entities and the way their performance is assessed internally, information provided to investors does not correspond to the manner in which the entity is managed, putting into question the relevance and the reliability of the information provided.

Therefore, we believe that the business model concept should be part of the revised Conceptual Framework consistently with the objective of the Conceptual Framework to provide decision-useful information to users. The application of the business model for recognition, measurement, presentation and disclosures should be implemented at the level of individual accounting standard, on a standard-by standard basis.

We note that insurance topics are discussed in Chapter 2 of RP in which IFRS 4 is cited by some as an example of an IFRS under development that could have benefited from the use of the business model and in Chapter 3 of the RP where an example relating to insurance is given.

Concerning the comments made in Chapter 2, we have long advocated in our comment letters on the various IASB's EDs on Insurance contracts and on Financial Instruments that it would not be appropriate to develop an accounting framework for insurers without taking into consideration their business model. In this respect, the interaction between insurance liabilities and their backing assets is at the core of the insurance activity and of its performance, and is illustrated through the asset liability management (ALM) strategies. As such, if the financial reporting does not reflect the ALM of insurers through a consistent measurement of their insurance liabilities and assets reflecting their overall linkage, the financial performance in the profit or loss would be obscured by short-term market fluctuations that reverse over time, putting into question the decision usefulness of information provided to users.

French insurers, and more general European insurers, are in the business of providing protection from risks and long-term savings products. These products result in predictable cash outflows, to a large extent, long-term. Insurers' investment strategies include diversified assets and are determined on the basis of the cash flow and risk profile of these "pooled" liabilities. ALM is a question of matching durations on a portfolio basis of different categories of assets in order to fulfil the obligations of the liabilities of the insurer towards policyholders. As such, insurers can make long-term investments as a consequence of a regular flow of premiums through an efficient ALM.

However, the business model of insurers has not been taken into account when developing the ED 2010 Insurance contracts causing confusion and misunderstanding among stakeholders. The IASB has developed some short term solutions to try to solve this issue. 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 were very positive steps in taking into account the overall linkage between insurance liabilities and their assets.

Nevertheless, it is still regularly opposed to insurers that there is a fundamental principle underlying IFRSs that assets and liabilities should be accounted for separately, as a convenient justification of why the IASB's proposals for financial instruments and insurance contracts are developed in isolation, e.g. without considering the ALM.

Indeed, the IASB's discussions on the insurance project continue without developing a real "asset/liability" accounting framework reflecting the business model of insurers. As a consequence,

- Either short term market fluctuations that are not part of the long-term performance of insurers would still be recorded in profit or loss instead of being recognised in OCI as:
    - The use of OCI is too restrictive. Limiting the FV-OCI category to simple debt instruments denies the fact that ALM strategies manage diversified categories of assets for the benefits of policyholders and not only "simple" debt instrument; in the same manner, the use of OCI should also be extended to include the derivatives used by insurers to manage interest rate risks or credit exposures of their portfolios of insurance liabilities or financial assets;

- Concerning equity instruments, if they are measured on a FV-OCI basis, as long as recycling is not permitted, realised gains and losses and impairment would not be part of the performance of the related insurance portfolios. On the opposite, if they are measured on FV-PL basis, short-term volatility fluctuations would obscure the performance in the profit or loss;
- Concerning the options and guarantees embedded in participating insurance contracts that are measured as part of the insurance contract liabilities at current fulfilment value, the IASB still considers that their nature is akin to that of a "financial" derivative and as such that the changes in their values should be recognised in profit or loss. These changes should be presented in OCI in the same manner as the changes in discount rates for insurance liabilities. Otherwise, the proposed IASB's treatment would lead to the recognition of short-term market fluctuations in the profit or loss that are not representative of the long-term operating performance of the insurer.

- Or accounting mismatches would continue to arise as long as for insurance liabilities that are asset dependent, that dependency is not appropriately reflected in the profit or loss through the use of a discount rate that reflects the ALM for the related portfolios of contracts irrespective of arbitrary distinctions between the features of the related insurance contracts.

Therefore, as long as the accounting framework for the insurance project is not developed with the objective of a consistent measurement of the assets and the insurance liabilities in line with their business model, it will not result in a meaningful profit and loss reflecting the economic performance of the insurers. As such, information provided in the financial statements will be artificially disconnected from the economic performance of the insurance activities.

Concerning the insurance example provided in Chapter 3, we believe that this example does not illustrate different business models but rather describes two different insurance products: non-participating versus participating contracts with different risk characteristics and profit-sharing features. The "business model solution" for insurance proposed in the RP seems to us to be an over-simplified approach to a much more complex topic as it does not take into account the overall linkage that exists between the insurance liabilities and the assets of the insurer irrespective of the existence or not of an contractual link.

Should you have any queries about the comments in this letter please do not hesitate to contact Bertrand Labilloy at + 33 1 42 47 93 58.

Yours sincerely,

Bertrand Labilloy
Director Economic and Financial Affairs