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THE DIRECTOR GENERAL

Brussels, 24 November 2003

Dear Sir David,

Please find enclosed CEA's comments on the Exposure Draft "Fair value hedge accounting for a portfolio hedge of interest rate risk".

CEA supports the Board in its decision to investigate how IAS 39 may be amended to take into account the fair value hedge of the interest rate risk on a macro-basis (portfolio basis). Insurance companies define and adjust their investment policy in order to match their liabilities towards policyholders. They aim at perpetuating this matching and securing the expected pattern of financial revenues that will enable them to honour their commitments to policyholders throughout the lifespan of these existing and expected liabilities. Insurance companies notably tend to cover their portfolio exposed to the interest rate risk. This hedging is globally appreciated on a macro basis as insurance companies mutualise and manage risks on a portfolio basis. It would also not be financially efficient nor possible to do so an individual basis i.e. on a policy basis.

However CEA would like to mention certain points specifically relating to the insurance business which should be taken into account for the finalisation of this project:

- Until Phase II is finalised, insurance companies will tend to account for most of their liabilities under local GAAPs according to the current proposition in ED5. As a consequence, in certain countries an important part of the business will be accounted for on a basis relatively similar to amortised cost. Since fair value of these liabilities has not yet been addressed by the IASB, no common view or interpretation of this concept for technical liabilities exists. Therefore, the proposed macro hedging in the exposure draft, despite being in principle of some interest to reflect the asset/liability management of insurers would not be of any help during Phase I (ED5) where the fair value of most technical liabilities is not required.

Sir David Tweedie
Chairman
International Accounting Standards Board
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- In line with our comments on ED5 – Insurance contracts, we question whether the rule exposed in question 2 (a) relating to the fair value of a financial liability with a demand feature is also applicable to the financial contracts underwritten by insurers. Indeed, in the ED5 comments, CEA strongly recommends that the Board examine its assessment of how the fair value of a financial instrument with a surrender option issued by an insurance entity should be accounted for. Indeed, such contract, even if accounted for as a financial instrument, is of a different nature than a simple deposit account due to its specific features (participating features, recurring premiums, long maturities etc…). Therefore, its surrender value should not be considered as the floor for any measurement of the liability resulting from such a contract. Should the tentative decision reached for core deposits (i.e. that the fair value of these financial liability with a demand feature could not be less than their redemption value) be extended to contracts issued by insurers, then insurance companies could not properly account for macro-hedging because the underlying measurement of the hedged item would not reflect its true and economic fair value.

- CEA noted that the designation of an overall net position is prohibited (IAS 39, Paragraph 133). Indeed, under the current proposal, the hedging must be applied by selecting a portion of either the assets or the liabilities corresponding to the amount of the hedged net position. CEA would like to stress that this treatment is not consistent with the practices of insurance companies when managing assets and liabilities.

- As already mentioned, it is clear for CEA that the IAS 39 and the ongoing improvements are not drafted taking into account the specificities of insurance business. For example, the project does not address the macro hedging of other financial risks that insurance companies face. Indeed, insurance companies tend to hedge on a macro basis the fair value of their stock portfolio, notably through the combination of options on stock indexes. These types of elements should be addressed but could be part of the Phase II discussions.

As we are committed to continue the constructive dialogue with the Board concerning specific insurance matters, we would like insist that the points raised above should be part of the Phase II discussions.

In the meantime, we are grateful for your consideration of our positions and would be happy to provide further information should this prove useful.

Yours sincerely,

Signed

Daniel Schanté	Patricia Plas
Director General	Economics & Finance Director