

Allianz Group

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Ref.: **Allianz comment letter on Proposed Statement of Financial Accounting Standards:
The Fair Value Option for Financial Assets and Financial Liabilities**

Dear Mr. Smith

Allianz Group appreciates the opportunity to comment on the Exposure Draft of Proposed Statements of Financial Accounting Standards, The Fair Value Option for Financial Assets and Financial Liabilities, including an amendment of FASB Statement No. 115.

Allianz Group supports the FASB and IASB convergence efforts and therefore highly appreciates the elimination of currently existing difference between the two accounting regimes. Allianz Group strongly supports the proposals in the Exposure Draft. From our point of view the fair value option represents an improvement in the external financial reporting, due to the following reasons:

- It helps to avoid accounting mismatches resulting from the mixed measurement model in the accounting standards for financial instruments,
- it reduces the complexity under US GAAP. Especially it improves the possibility to reflect the economic hedging of certain risk exposures in the external reporting without using hedge accounting and
- it mainly supports the convergence between IFRS and US GAAP.

Despite the efforts to achieve convergence between IFRS and US GAAP we support the proposal, that usage of the fair value option is not limited to particular situations like in IAS 39.

Issue 1: Financial Instruments included in the scope of the Exposure Draft

Allianz Group agrees that the fair value option should apply to the financial assets and financial liabilities included in Issue 1. With respect to the inclusion of insurance contracts, we strongly support the inclusion in the scope of the present proposed fair value option as an opportunity to avoid potentially differences between IFRS and US GAAP.

Issue 2: Firm commitments involving only financial instruments

Allianz Group agrees that firm commitments involving only financial instruments should be included in the scope of the fair value option, as this reduces the complexity and administration burden of hedge accounting. Especially in the insurance business the reinvestment risk needs to be strongly considered and the proposed Fair Value option helps to reduce the accounting mismatch.

Issue 3: Scope exclusion for loan commitments and demand deposits

We would support to include all loan commitments in the scope of the proposed fair value option already in phase 1. There is no substantial economic difference between loan commitments currently in the scope of SFAS 133 and those outside SFAS 133. The application of the fair value option for loan commitments that do not meet the definition of a derivative of SFAS 133 is essential for the reduction of complexity and potential income statement mismatches. In addition this supports convergence with the relevant rules under IFRS.

Given that the legal maturity, instead of the economic maturity of demand deposit accounts, is relevant for accounting purposes we consider a mark-to-market valuation on a single-account base not appropriate as it would not reflect the effective value of the demand deposits in a financial institution. In fact the demand deposit accounts represent a value which could only be reflected appropriately in case the accounts would be measured on a portfolio basis. For these purposes internal valuation models are already existing and economic hedging considers the value. Thus, a income statement-mismatch will arise, if a financial institution follows best practice risk management and uses financial derivatives to hedge the interest rate risk exposure from core deposits. Therefore, it should be discussed if and how the fair value of the core deposits as an asset could be reflected in the balance sheet.

Issue 4: Other scope exclusions

Allianz agrees to expand the scope exclusion to the listed items in Issue 4.

Issue 5: Items to address in Phase 2

Allianz suggests to include property investments in the scope of the fair value option in Phase 2 of the project. Especially for insurance companies as well as for other institutional investors property investments are part of the over-all capital investments and there is no substantial difference made to financial investments. If all assets including property are managed on a fair value basis there should be the possibility to reflect this on the balance sheet as well. In addition this would result in a further elimination of differences between IFRS and US GAAP.

Issue 6: Own Credit Spread

The proposed Statement would permit an entity to apply the fair value option for certain financial liabilities, including debt liabilities. An issuer who has elected the fair value option for its debt liabilities would report all changes in the fair value of those liabilities - including fair value changes resulting from changes in the issuer's own creditworthiness - as gains and losses in earnings. The inclusion of an entity's own credit risk in the fair value measurement of liabilities causes misleading income statement- and balance sheet-figures. Unlike hedge accounting an undesirable consequence of the fair value option is that (own) credit risk will cause the profit and loss reflecting an economically not existing volatility.

For liabilities (e. g. long-dated, liquidity providing issues) which lack any short-dated trading intention the shown movement in the respective market values cannot be realised by corresponding hedging or buy-back activities and thus do not represent "real" profit or loss figures. The reported income statement-swings due to changes in own credit spread are misleading for any external stockholder in the entity. As long as the going concern assumption applies to the reporting company the own creditworthiness will not be reflected in future cash flows and should therefore not change the fair value of the financial liability. Therefore the potential benefit of the fair value option to stabilise profit and loss (especially where hedge accounting cannot be applied) will be distorted. We also support the corresponding concerns of prudential regulators (e. g. BASEL Committee).

Issue 7: Presentation and disclosure guidelines

Allianz agrees with the presentation and disclosure guidelines in the Exposure Draft. Nevertheless we think that we would object a to detailed, rule based guidance on how amounts should be classified and reported either on the face of the balance sheet or in the notes.

We would be pleased to discuss our comments with you.

Yours sincerely,

Dr. Helmut Perlet
Member of the Management Board
and Chief Financial Officer