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Comment on the FASB's Proposal for Principles-Based Approach to U.S. Standard Setting

Ladies and Gentlemen.

please find attached the comment of Allianz Aktiengesellschaft on the FASB's Proposal for Principles-Based Approach to U.S. Standard Setting. The letter has already been sent to you by electronic mail. We hope that you find our comments helpful and we would be pleased to discuss them with you at your convenience.

Sincerely,
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Dr. Susanne Kanngiesser Head of Group Accounting

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Comment Letter to the IASB of Allianz Aktiengesellschaft on the Exposure Draft of proposed amendments to IAS 32 and IAS 39

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15 January 2003

Re: Proposal For Principles-Based Approach to U.S. Standard Setting

Ladies and Gentlemen:

Allianz appreciates the opportunity to comment on the FASB's proposal to adopt a principles-based approach to U.S. standard setting. Overall, we support the FASB's initiative to reassess the effectiveness of its approach to setting accounting standards and believe that a principles-based approach will improve the quality and transparency of financial reporting while minimizing the current complexity of the accounting standards. However, we also recognize that the conversion to a principles-based approach encompasses many pitfalls which must be carefully identified and considered prior to proceeding and that supplemental measures adopted by the FASB and SEC will most likely be necessary to ensure that the conversion to this approach is successful.

Before addressing the specific issues outlined in your proposal, we would like to highlight that we strongly recommend that the activities concerning the adoption of a principles-based approach to U.S. standard setting be closely coordinated with the US GAAP / IAS convergence project. Successful convergence of IAS and US GAAP is of primary importance to the preparers and users of financial statements. The concept of convergence should always be kept at the forefront of any discussions concerning amendments to existing standards or the promulgation of new standards.

We have the following responses to the specific issues raised in your proposal:

1. Do you support the Board's proposal for a principles-based approach to U.S. standard setting? Will that approach improve the quality and transparency of U.S. financial accounting and reporting?

As a user of International Accounting Standards (IAS) as our primary accounting basis for reporting our consolidated group financial statement information, we have experienced the benefits and drawbacks in using principles-based accounting standards. We also have experience, as an SEC foreign registrant, with the application of U.S. accounting standards and disclosure requirements. As stated above, we support a principles-based approach. We believe a detailed rules-based system without governing principles is prone to manipulation by structuring transactions that meet the criteria of the rules, but fail to meet the purpose and principle of the accounting standard.

Over the years, the general nature of the IASB principles-based approach has allowed for different interpretations of its standard. In concept, this is conducive to allowing a company the proper flexibility to present the true substance of its results of operations without being

subject to specific rules which do not capture the economic essence of its transactions. However, in practice, more defined rules and interpretations provided by other regulatory and accounting standards bodies have been utilized in interpreting the general principles of IAS. In effect, these more specific rules have had a profound influence in the shaping of the application of IAS principles-based standards. This situation highlights one of the potential pitfalls with a principles-based system which is that interpretations of these principles by large public companies, legal judgments and the SEC will likely replace the interpretive guidance that was previously provided by the FASB without, perhaps, going through the FASB's due process. Therefore, it is important that any principles-based approach to standard setting is supported by the SEC and legal systems. This would entail that the SEC, as part of its public policy, declare that it will support all reasonable interpretations of a principle-based standard that meets the core principles of properly transmitting relevant, reliable information of the economic substance of a transaction.

2. Should the Board develop an overall reporting framework as in IAS 1 and, if so, should that framework include a true and fair view override?

A clear, internally consistent overall framework is crucial to building a coherent set of standards that captures the overriding principles of consistency and relevance and presents a fair picture of economic reality. The framework should avoid rendering judgments concerning whether fair value or historical cost is the proper valuation technique since this is beyond the scope of such a high level framework. Whether fair value or historical cost is the appropriate measure should be considered within the individual standards rather than established as a governing principle. Instead, for example, the governing principle should be that the proper valuation of an asset or liability should be based on its utility resulting from its intended use within the operations of a going concern.

Additionally, this framework should include concepts concerning financial statement disclosures to ensure that disclosures required by accounting standards will be understandable, relevant, and useful. The area of disclosure should not be considered secondary to recognition and measurement principles because of its importance to the financial statements. The emphasis should be on fewer disclosures of higher quality that meet the disclosure principles presented in the overall reporting framework. This will assist in reducing the static that currently exists due to the ever increasing volume of required disclosures.

The inclusion of a true and fair view override appears to be consistent with the Board's primary objective of presenting information that faithfully represents economic reality and is not viewed as a way to circumvent the established rules. Proper disclosure of instances where a company's accounting policy applies this true and fair view override will assist in mitigating the abuse of such a provision.

3. Under what circumstances should interpretive and implementation guidance be provided under a principles-based approach to U.S. standard setting? Should the board be the primary standard setter responsible for providing that guidance?

Interpretive and implementation guidance should be used to clearly illustrate the principles within a standard to ensure that standard is consistently applied in accordance with the objectives of the standard. This requires a significant degree of judgment since accounting themes differ in objectivity and complexity. For example, accounting for fixed assets may be considered less complex than accounting for intangible assets and, therefore, may require a different degree of interpretive guidance. Unfortunately, no perfect solution exists that can take into account all situations. Although the IASB is considered to take a principles-based approach to standard setting, IAS 39 is accompanied by a significant amount of implementation guidance. This, along with the numerous interpretations of FASB 133, appears to clearly show that certain issues such as derivatives require significantly more

guidance than other less complicated areas. However, the guidance provided should not be in such detail as to consider individual issues on a case by case basis, but rather to clarify the governing principles of the standards.

As stated in your proposal, much of the interpretive guidance was created as a result of queries posed by preparers and auditors about the proper way to account for particular transactions. We would submit that perhaps in all cases these queries were made in a good faith effort to comply with the principles of the particular accounting standard in question rather than to reach a particular accounting result. We, therefore, believe that there is value in providing interpretive guidance. However, a separate framework or philosophy should be developed to guide the Board on whether or not and to what extent implementation/interpretive guidance should be provided.

This framework should have the following characteristics:

Only one interpretive body controlled by the Board, such as the EITF, should be permitted to establish official interpretations of standards. This would promote consistency and control over the quality and volume of published interpretations and would reduce the time spent by preparers and users researching copious amounts of literature from other accounting bodies and determining which literature should take precedence. This would also assist the board in its efforts to minimize standards overload and decrease the complexities faced by international users who are less familiar with the US standards.

The EITF should work closely with its counterpart at the IASB, the International Financial Reporting Interpretations Committee, to ensure that the guidance provided by the EITF is consistent with the overall goal of convergence;

Guidance concerning specific issues should only be formally published by the Board in
when it clearly enhances the understanding of the principles of the standards and
significantly and appropriately enhances consistent application of the accounting
principle. The emphasis of the guidance should be the clarification of the intent of the
principle and not the establishment of criteria that would result in a rules-based
accounting principle.

We would anticipate that the amount of interpretive guidance resulting from this framework would be less than that provided in the past and less detailed in nature.

4. Will preparers, auditors, the SEC, investors, creditors, and other users of financial information be able to adjust to a principles-based approach to U.S. standard setting? If not, what needs to be done and by whom?

We, as preparers, understand that we would have significantly more responsibility for making decisions concerning the evaluation and interpretation of accounting standards under a principles-based system as compared to a rules-based system. However, we firmly believe that we have a far greater intimate knowledge of the true economics of our transactions and, therefore, are in the best position to make judgments concerning the accounting and disclosure of these transactions. We also act in the capacities of an investor and creditor as part of daily business operations. From each of these perspectives we believe that we would be able to adjust to a principles-based approach because it would provide a more accurate and transparent picture of our investees' and borrowers' financial statements. This approach, of course, would expected to be accompanied by appropriate disclosures concerning companies' accounting policies and how their policies deviate from accounting standards due to the application of true and fair view overrides.

We are obviously unable to comment from the SEC's and auditors' perspectives. However, we believe that the SEC and auditors, along with preparers and the FASB must work in

concert in order to properly effect the change from the current rules-based approach to a principles-based approach. If the FASB and the preparers adopt a principles-based approach which is not adequately supported by the SEC and auditors, the conversion to a this approach will not succeed.

5. What are the benefits and costs (including transition costs) of adopting a principles-based approach to U.S. standard setting? How might those benefits and costs be quantified?

From a preparer's perspective the level of costs would reflect the number of changes made to existing standards. There would also be additional costs incurred in evaluating new standards given the requirement to utilize more analysis and judgment in determining and developing the proper accounting treatments that are consistent with the principles outlined in the new standards. These costs would be offset in part by eliminating, in certain cases, detailed analyses of particular nuances of contracts and transactions where the true economics of these contracts and transactions are clearly understandable. Additionally, a clearly communicated, well designed transition plan by the FASB would also allow companies to more efficiently and effectively plan its activities to convert to the new approach.

6. What other factors should the Board consider in assessing the extent to which it should adopt a principles-based approach to U.S. standard setting?

Exceptions

The Board should continue to consider the use of exceptions in drafting its standards due to the significant differences that exist among the economic models of certain industries and professions (e.g. investment banking versus insurance). It is important that industry differences are recognized in drafting standards in order to present the true economic reality of a company in that industry.

IAS / US GAAP convergence

As mentioned in our opening comments, it is important that the impact on the IAS / US GAAP convergence project be considered during any deliberations concerning amendments to existing standards or the development of new standards. We believe that the spirit of this proposal is consistent with the goal of harmonizing the two accounting bases. We request that the Board continue to consider convergence as a primary factor throughout this proposal process.

We would be pleased to discuss our comments with you at your convenience.

Dr. Helmut Perlet

Member of the Management Board

Dr. Susanne Kanngiesser Head of Group Accounting

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