May 15, 2013

Ms. Susan M. Cosper, Technical Director
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

Re: File Reference No. 2013-220

Dear Ms. Cosper:


Cigna Corporation appreciates the opportunity to comment on the Financial Accounting Standards Board’s (FASB) Exposure Draft (ED), “Recognition and Measurement of Financial Assets and Financial Liabilities.” Cigna is one of the largest investor-owned health care and related benefits organizations in the U.S., and has operations in selected international markets. As of March 31, 2013, Cigna held $47 billion of assets (excluding separate accounts) with approximately 50% comprised of investment assets, primarily debt securities and commercial mortgage loans. Given this investment portfolio, Cigna's management team is both a user and preparer of financial information on a daily basis. Our comments represent the joint perspectives of our investment professional users and accountants/preparers.

Cigna supports the goal to increase investor confidence in financial reporting by improving and simplifying reporting for financial instruments, as well as convergence efforts towards higher quality accounting and reporting standards together with the International Accounting Standards Board (IASB). In our view, communication with investors and analysts through the basic financial statements should be simple and direct, with the goal of helping these users understand an entity’s current financial condition, periodic performance and prospects of future cash flows. We believe that the information conveyed should be consistent with how an entity manages its business and analyzes its performance. However, we believe that the ED does not fully accomplish the goal of improving and simplifying reporting financial statements, as well as ensuring relevant information for users.

Our chief concern is that the current classification criterion is too narrow as many debt instruments have features beyond “solely payments of principal and interest.” The current proposal continues to require many debt instruments to be measured at fair value with all changes reported through the income statement because of features that will not meet the solely payments of principal and interest criteria. As a result, the financial statements will not accurately reflect the operating performance of the business model used most frequently by many insurance enterprises, including Cigna. These views are described more fully under Recommendations 1 and 2 below. Recommendations 3 through 6 are intended to improve the application of the proposal.
In summary, these views are as follows:

- The assessment of contractual cash flows should result in investments with significant principal and interest, despite other features with insignificant cash flow impacts, to be classified and reported at fair value through other comprehensive income or amortized cost.
- The definition of principal should be expanded to include the repayment amount at maturity or other settlement to ensure that financial assets purchased at a premium or a discount or those with prepayment options pass the contractual cash flow characteristics test.
- Implementation guidance for allowable sales of instruments classified as amortized cost should be broadened and converged with the IASB’s ED, “Classification and Measurement: Limited Amendments to IFRS 9.”
- The unconditional fair value through net income option from existing U.S. GAAP should be retained.
- Foreign currency transaction gains and losses on foreign-currency-denominated financial instruments should continue to be reported in other comprehensive income as currently required by U.S. GAAP.
- The effective dates of final guidance for financial instruments from the FASB and IASB should be converged, and considered in the implementation plan for any final insurance contracts standard.

**Recommendation 1:** The assessment of contractual cash flows should result in investments with significant principal and interest, despite other features with insignificant cash flow impacts, to be classified and reported at fair value to other comprehensive income or amortized cost. *(ED Questions 3, 4, 7, 9)*

We believe the criteria to assess if beneficial interests in securitized financial assets are solely payments of principal and interest is too restrictive. Similar to our strategy for plain vanilla debt securities, and consistent with our business model, Cigna purchases structured investments to realize ongoing, enhanced annual yield (principal and interest). For these structured investments, Cigna measures management’s performance based on its ability to collect the instruments’ contractual principal and interest. Therefore, it is our view that these instruments should be classified at amortized cost or fair value through other comprehensive income to best reflect our business model and economic performance.

For example, certain structures may be supported by expected underlying cash flows from leasing or other contractual arrangements that may not be considered basic loan features, and therefore fail the solely payments of principal and interest test. Cash flows from these structures are generally fixed and determinable, however, interpretation of whether this meets the contractually linked criteria may result in different accounting treatment than similar economics associated with corporate debt. We understand the purpose of the proposed cash flow assessment is to determine the appropriate classification for the instrument in its entirety. Therefore, we believe it will not be meaningful to classify and measure this subordinated instrument at fair value through net income due to a feature that does not significantly change contractual cash flows and that otherwise would be classified in amortized cost or fair value to other comprehensive income. Further, reporting investments in structured securities at fair value through net income could result in significant earnings volatility that could be viewed negatively by investors. We believe that significant payments of principal and interest provide an adequate gauge for contractual cash flow analysis and suggest incorporating an insignificance test for all features (as used for the modified economic relationship) to assess if the securitization or loan significantly achieves the criteria of “solely payment of principal and interest.” A single defined measurement approach will assist preparers and auditors to consistently and more simply interpret and apply the contractual cash flow assessment.
We are also concerned with the proposed guidance that requires measurement at fair value through net income if the credit risk of the underlying pool of financial instruments inherent in the tranche held for investment is lower than the exposure of the credit risk of the aggregate underlying pool of financial instruments. We disagree with this philosophy as payments to each tranche holder represent payments of principal and interest from the underlying loans, and find this constraint inconsistent with the purpose of the proposed cash flow assessment to classify the instrument in its entirety. We further disagree with introducing credit considerations into the proposed model that classifies financial instruments based on the entity’s business model and an instrument’s contractual cash flows. We recommend that FASB remove these eligibility criteria for classification at fair value through other comprehensive income.

**Recommendation 2:** The definition of principal should be expanded to include the repayment amount at maturity or other settlement to ensure that financial assets purchased at premium or discount or those with prepayment options pass the contractual cash flow characteristics test. *(ED Questions 5, 6)*

825-10-55-21 paragraph b proposes that contractual cash flow characteristics can include prepayment amounts that **substantially represent** unpaid amounts of principal and interest, which may include **reasonable additional compensation for the early termination of the contract.** However, the proposed guidance does not define or provide examples of “substantially represent” or “reasonable, additional compensation.” We also note that principal is defined within the ED as the amount transferred by the holder at initial recognition. A strict application of this proposed description would potentially cause debt instruments purchased at a premium or a discount and repayable at par plus accrued interest to fail the solely payment of principal and interest test. This outcome seems inconsistent with the intent of the Board to simplify the measurement and presentation of financial instruments in financial reporting.

Also, most of Cigna's investments in private placement debt securities and commercial mortgage loans, as well as an increasing number of newly issued public debt securities, contain market-based prepayment penalties. These prepayment penalties are “make-wholes” that are conceptually similar, although generally not equal, to the foregone interest that would have been collected had the issuer not elected to retire their debt early. Such make-wholes are an industry standard in the U.S., are an economic disincentive for the borrower to restrict prepayment activity to non-economic events, and are a protection for Cigna's investment value if prepayment is elected by the issuer when interest rates have fallen. The calculation of these make-wholes are determined at issuance and are exercised at the issuer's option—indicating that such compensation is considered reasonable by the issuer for an early settlement date. Our view is that such prepayment options are reasonable additional compensation for early termination and are a typical market practice in the U.S. markets for private debt securities and commercial mortgage loans, and thus are consistent with the definition of “solely payments of principal and interest”.
Our interpretation of the ED is that if make whole compensation for termination is not considered reasonable, we would be required to classify and measure our debt securities and commercial mortgage loans with make whole provisions at fair value through net income. While the FASB Insurance Contracts exposure draft has yet to be re-exposed and finalized, we understand that according to tentative decisions reached, changes to insurance contract liabilities attributable to changes in discount rates will be presented in other comprehensive income. Consequently, an accounting mismatch will result between investment assets’ fair value changes in net income and insurance liabilities’ interest rate valuation changes in other comprehensive income. The resulting artificial volatility in net income will not provide investors with useful or relevant financial information about the results of operations of many insurance enterprises. Furthermore, investor confidence and competition for capital will be compromised as this financial information will not provide decision-useful information to assess the amounts, timing and uncertainty of cash flows for many insurance enterprises. We do not believe users desire or will benefit from such financial reporting that produces artificial volatility.

We believe that most commercial mortgage loans and private placement debt securities should be classified and measured at amortized cost under the ED if the business model is to hold them for the collection of contractual cash flows. We recommend that the proposed guidance be clarified to specify that market terms, including prepayment penalties, should be considered in determining “reasonable compensation for early termination.” We further suggest that FASB expand the definition of principal to include the repayment amount at maturity or other settlement to ensure that financial assets purchased at a premium or a discount or those with prepayment options pass the contractual cash flow characteristics test.

**Recommendation 3**: Implementation guidance for allowable sales of instruments classified as amortized cost should be broadened and converged with International Accounting Standards Board’s (IASB) Exposure Draft (IASB ED), “Classification and Measurement: Limited Amendments to IFRS 9” *(ED Question 12)*

Cigna supports the proposed changes that do not appear to contain a tainting provision if amortized cost investments are sold for acceptable specified reasons. We agree that the exercise of professional judgment is superior to the introduction of a prescriptive tainting concept. However, although paragraph 825-10-55-32 provides examples of sales activity that would not call into question management’s strategy, we recommend the guidance be broadened to recognize that business is dynamic and demands that investment strategies that change in reaction to external factors such as acquisitions and divestitures and regulatory mandates are not necessarily “very infrequent”. While the business model test for the fair value through other comprehensive income classification category has a balanced composition of assets managed to collect contractual cash flows and those managed for sales, the proposed business model for amortized cost appears to allow sales in only very limited scenarios. The risk is that such instruments will be required to be measured at fair value through other comprehensive income even though amortized cost provides the most useful information for such assets.

We also note that the application guidance of FASB’s ED states that such sales are to be “very infrequent” versus the proposed IASB’s language that sales are to be “infrequent.” Cigna experienced the arduous implementation process for ASC 320 that resulted in numerous practice issues and several iterations of clarification guidance following the adoption of that standard. Ultimately, many insurance enterprises determined that few portfolio management practices could meet the ASC 320 threshold of “very infrequent” sales, causing portfolio tainting and they abandoned the amortized cost category entirely. We are especially concerned that implementation of the current FASB and IASB proposals will emerge with dissimilar results, putting U. S. companies at a competitive disadvantage with their global industry peers. The FASB and IASB
should work together to converge this guidance to the IASB’s view of “infrequent” sales and no portfolio tainting to increase comparability and consistency of application.

**Recommendation 4:** The unconditional option to fair value through net income from existing U.S. GAAP should be retained. *(ED Questions 15, 21, 37)*

We support an unrestricted option to fair value through net income rather than the proposed limited circumstances of the ED. We prefer the existing U.S. GAAP guidance that permits application of the fair value option to many more financial instruments. We believe that an unrestricted option will be useful for many entities that may not want to apply complex hedge accounting requirements, or for entities that prefer to carry their investments at fair value to the income statement in certain situations that it is believed to yield more decision-useful information to investors. An unrestricted option is also consistent with the fact that measurement through FVNI is considered the residual category in the FASB ED. We believe it will enable preparers to select a fair value measurement basis in circumstances when it logically provides more decision-useful information to investors and other users.

**Recommendation 5:** Foreign currency transaction gains and losses related to foreign-currency-denominated financial instruments should continue to be measured and reported in other comprehensive income as currently required by U.S. GAAP. *(ED Question 26)*

We disagree with the proposed amendment that will change the measurement and presentation requirements for foreign currency gains and losses relating to foreign-currency-denominated financial instruments that are measured at fair value through other comprehensive income. In cases when a financial instrument has met the fair value through other comprehensive income measurement requirements, we believe that the entire change in value, including foreign exchange impacts, should be consistently presented. Separating foreign exchange gains and losses and reporting these values in net income will improperly imply that such gains and losses have been realized; this is not consistent with the simplification objective of this measurement classification. This concept also does not achieve the objective of providing more useful information to investors.

Regarding the fair value-based requirement for computing foreign currency gains or losses, we strongly disagree with this proposed amendment. Although the Board has noted in reference to Investment Companies in BC299 that there is no single right answer to determining an allocation of the components of fair value changes, management does not ignore the foreign currency element of value in their decisions. As there are many factors that drive fair value, a prescribed methodology for calculating foreign currency gains and losses based on fair value introduces an additional variable to the equation that does not achieve a truer economic answer. Because changes in foreign currency spot rates are the key variables that drive foreign exchange gains and losses, we believe that these variables should be applied to a cost-based constant to achieve the most economically valid measurement. Given the complexities that already exist in disaggregating foreign currency gains and losses, we find the proposed approach to be operationally difficult, and expect that not only will it require an entity to modify its processes and information systems, but will also demand further engagement with attendant increased costs for those many enterprises that use external pricing vendors. This approach may also cause further divergence from international accounting standards as the recent IASB ED requires amortized cost as the base for this measurement. We believe this proposal fails to achieve the objective of reducing the complexity of accounting for financial instruments.
Recommendation 6: The effective dates of final guidance for financial instruments from the FASB and IASB should be converged, and considered in the implementation plan for any final insurance contracts standard. *(ED Questions 32, 33)*

- We urge the Board to align the effective date for a final standard for financial instruments with the final amendments to IFRS 9 so that both standards are implemented in the same timeframe and manner.
- We believe the single effective date chosen should provide adequate time for companies to prepare for the many assessments needed to classify thousands of instruments held by insurance and financial services enterprises and changes systems, reporting and controls that these new standards will demand.
- We urge the Board to align the effective dates for a final standard for financial instruments with any final standard for insurance contracts, or provide for reassessment of the business model and reclassification of financial instruments supporting insurance books of business when any insurance contracts standard is implemented.

If we can provide further information or clarification of our comments, please call me (215-761-1170) or Nancy Ruffino (860-226-4632).

Sincerely,

Mary T. Hoeltzel