2012-200
Comment Letter No. 156

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Technical Director
File Reference No. 2012-200
Financial Accounting Standards Board
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Via E-mail: director@fasb.org

RE: *Proposed Accounting Standards Update – Disclosures about Liquidity Risk and Interest Rate Risk*

The American Insurance Association (AIA) appreciates this opportunity to provide comments on the Proposed Accounting Standards Update - *Disclosures about Liquidity Risk and Interest Rate Risk*. AIA represents approximately 300 major U.S. insurance companies that provide all lines of property-casualty insurance to U.S. consumers and businesses, writing more than $117 billion annually in premiums. AIA members support the goal of improving disclosure to provide decision-useful information about an entity's liquidity and interest rate risks when those risks are significant to the entity. However, it should not be assumed that entities from all financial sectors manage assets and liabilities in the same manner. The proposed update assumes liquidity and interest rate risks are major considerations, and does not acknowledge that there are certain businesses that are not subject to high degrees of either risk. We believe the proposed update would be greatly improved if the final guidance were stated as a principle that is based on the business activity of the entity rather than the type of entity.

Characteristics of P&C Insurance Liabilities

The business model for property and casualty insurance companies is significantly different than the business model for financial institutions, such as banks and life insurance companies. Liquidity is not generally an issue for property and casualty insurers, as the operating cash flows (premiums received along with interest income and investment maturities, etc.) adequately cover claims payments, other operations, and capital activities (e.g., dividend payments, share buybacks, redemption of debt) without the need to sell investments. Even with large claims settlements or large catastrophes, sales of investments are generally not necessary since the insurer has adequate time to plan for the future disbursements (i.e., increase short term holdings).

As a result, the management of the investment portfolio is based on a strategy that maximizes returns without undue risks, given the uncertainty with our insurance liabilities. Property and casualty insurers do not perform asset/liability matching, but instead manage the overall duration of invested assets. The composition of the investment portfolio has less risk and is of shorter duration than other financial institutions. Generally, the portfolio is constructed with relatively safe, highly liquid securities, such as U.S. government, municipal securities, investment grade corporate securities, and a significant amount of short-term investments. Also, claims liabilities are generally not interest sensitive; they arise as the result of external events that trigger a financial cost, as provided under the terms of the insurance contract. Also, the amount of that liability is not driven by interest rates. In some lines – liability for example – the ultimate cost driver may actually be social inflation (deflation), where previous jury awards may drive up (down) that cost.

In short, the goal of the property and casualty insurance business model is to maintain a positive cash flow that allows us to meet our current cash needs from operating cash flows, while maintaining a high level of capital as compared to other financial institutions. This characteristic is unlike bank accounts, certificate of deposits, or whole life, variable life and annuity products, where the insurer invests the cash received with the goal of making more investment income than the expected future payouts owed to the policyholders. Property and casualty insurers, on the other hand, are significantly less leveraged, have no call risk, do not have liquidity issues due to the current cash flow from operations and the availability of highly liquid assets, and hold higher amounts of capital due to the potential for significant adverse events.

In summary, property and casualty insurance companies generally are distinguished from other financial institutions by the following characteristics:

- Hold higher levels of capital due to the inherent risk of potential future adverse events, incurring a lower rate of return on capital
- Limit asset risk by holding a higher quality and more liquid investment portfolio
- Manage overall duration of invested assets, rather than formal asset/liability matching
- Satisfy claims, other expenses, and capital activities out of current operating cash flow, rather than building long-term assets to satisfy future claim payments. Thus, claims are expected to be satisfied primarily through cash from operations without the need to liquidate assets.

Because of the above-identified differences, AIA encourages the Financial Accounting Standards Board (FASB) to consider removing property and casualty insurers from the scope of the proposed update, or to structure the new guidance as a principle that is based on the business activity of the preparer, rather than the type of business entity. As an alternative, the FASB could defer action at this time and consider what disclosures would be appropriate for an insurer within in the context of the Insurance Contracts project.

AIA Response to Certain Questions

Question 1: For a financial institution, the proposed amendments would require a liquidity gap table that includes the expected maturities of an entity's financial assets and financial liabilities. Do you foresee any significant operational concerns or constraints in complying with this requirement? If yes, what operational concerns or constraints do you foresee and what would you suggest to alleviate them?

AIA Response: *We do not believe that property and casualty insurance companies should be considered financial institutions as it pertains to the proposed amendments for many reasons which are outlined below. Liquidity is not an item of significance to users of property and casualty financial statements, since the servicing of loss claims, operating expenses, and capital activities are usually satisfied from the cash flow provided from operations.* In addition, p*roperty and casualty insurance liabilities do not* have *contractually prescribed maturities. Unless an insurable event occurs, there will be no "maturity" for any given contract. When there is a loss and a subsequent claim, the amount to be paid out may be subject to negotiation, litigation, and other variables; thus, disclosing a projection based on these significant uncertainties would not provide decision-useful information. Given these facts, the liquidity gap table could be misleading to users of property and casualty insurance companies financial statements because it is not representative of our business model.*

There would be severe operational concerns with respect to the "Incurred But Not Reported" (IBNR) portion of insurance liabilities. IBNR is an estimate of potential liability, based on the fact that an event has occurred that would likely affect policyholders. That estimate is made in anticipation that claims will eventually be submitted for the event losses. However, there are no specific claims to back up the IBNR estimate, so a meaningful projection of payments based on this estimate would not be possible. Layering uncertainty onto another uncertainty would not provide decision-useful information. In addition, we are greatly concerned with the interim reporting requirement not currently required in the SEC's MD&A disclosures for aggregate contractual obligations, as well as, the extensive number of arbitrary time periods required by the proposed disclosures.

It should be noted that insurers subject to U.S. insurance regulation are already obligated to publicly disclose detailed information about their investments each year. Thus, the proposed disclosure is not necessary with respect to the asset side of such insurers' balance sheets.

Question 2: For an entity that is not a financial institution, the proposed amendments would require a cash flow obligations table that includes the expected maturities of an entity's obligations. Do you foresee any significant operational concerns or constraints in complying with this requirement? If yes, what operational concerns or constraints do you foresee and what would you suggest to alleviate them?

AIA Response: *It cannot be emphasized enough that property and casualty insurance products are significantly different than the products offered by other financial services sectors. For*

purposes of the proposed update, then, a property and casualty insurer should, in general, be viewed as "not a financial institution". Assuming such a categorization, the suggested disclosure would nonetheless be problematic because this industry's liabilities do not contain prescribed maturity dates. Preparing the proposed schedule would require the insurer to make a prediction as to when a liability might be settled. We acknowledge that SEC Registrants currently report claims liabilities in the contractual obligations tables, but we also note the significant amount of disclaimers that accompany the table.

We again echo the comments from above in question 1. We are concerned with the interim reporting requirements versus the current annual requirement by the SEC, as well as the extensive number of arbitrary time periods required by the proposed disclosures. We do not believe there are any benefits to these disclosures that would outweigh the operational costs to produce.

Question 3: The proposed amendments would require information about expected maturities for financial assets and financial liabilities to highlight liquidity risk. Expected maturity is the expected settlement of the instrument resulting from contractual terms (for example, call dates, put dates, maturity dates, and prepayment expectations), rather than an entity's expected timing of the sale or transfer of the instrument. Do you agree that the term expected maturity is more meaningful than the term contractual maturity in the context of the proposed liquidity risk disclosures? If not, please explain the reasons and suggest an alternative approach.

AIA Response: *Liquidity is not a significant risk to property and casualty insurers due to the nature of insurance contracts and how the investment portfolios are managed.*

Question 4: The proposed amendments would require a quantitative disclosure of an entity's available liquid funds, as discussed in paragraphs 825-10-50-23S through 50-23V. Do you foresee any significant operational concerns or constraints in complying with this requirement? If yes, what operational concerns or constraints do you foresee and what would you suggest to alleviate them?

AIA Response: *We find this requirement to be unnecessarily redundant since publicly traded companies in the United States already disclose sources of liquidity in their filings with the U.S. Securities and Exchange Commission (SEC). As regulated entities, U.S. property-casualty insurers also file detailed schedules about their investments. Given that this information is part of the mix of information that is already available to the user, this proposed requirement appears to create more disclosure burden on the preparer without a demonstrated incremental benefit to the user. We also believe that the SEC required disclosures are better tailored for this type of information because disclosure within Management's Discussion and Analysis provides companies with the protection under the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 with regard to "forward-looking" statements.*

Question 6: As a preparer, do you feel that the proposed amendments would provide sufficient information for users of your financial statements to develop an understanding of your entity's exposure to liquidity risk? If not, what other information would better achieve this objective?

AIA Response: *In its current form, we do not believe the proposed guidance will improve user understanding of the liquidity risks of a property-casualty insurer because the guidance is framed more from the context of a bank or a life insurance company, rather than a property-casualty insurer.*

Question 13: The interest rate risk disclosures in this proposed Update would require a re-pricing gap table. Do you foresee any significant operational concerns or constraints in complying with this requirement? If yes, what operational concerns or constraints do you foresee and what would you suggest to alleviate them?

AIA Response: *Consistent with our earlier comments, the interest rate disclosure guidance assumes a banking business model – which is wholly different from that of a property and casualty insurer. Interest is not a driver of property and casualty insurance liabilities. Insurable loss events – the frequency and severity of which are beyond the control of the property and casualty insurer – occur regardless of the interest rate environment. Insurance reserves are the most significant liability on an insurer's balance sheet and a re-pricing gap table would have no relevance to that liability, and therefore provide no useful information.*

Question 14: The interest rate risk disclosures in this proposed Update would include a sensitivity analysis of net income and shareholders' equity. Do you foresee any significant operational concerns or constraints in determining the effect of changes in interest rates on net income and shareholders' equity? If yes, what operational concerns or constraints do you foresee and what would you suggest to alleviate them?

AIA Response: *We do not believe this information will provide decision useful information to users of property and casualty insurance company financial statements. Unlike banks and life insurance companies, most property and casualty insurers do not utilize interest rate management programs.*

Question 15: As a preparer, do you feel that the proposed amendments would provide sufficient information for users of your financial statements to understand your entity's exposure to interest rate risk? If not, what other information would better achieve this objective?

AIA Response: *We do not believe disclosures related to interest rate risk exposure are relevant for a property and casualty insurer.*

Question 21: Although the proposed amendments do not have an effective date, the Board intends to address the needs of users of financial statements for more information about liquidity risk and interest rate risk. Therefore, the Board will strive to make these proposed

amendments effective on a timely basis. How much time do you think stakeholders would require to prepare for and implement the amendments in this proposed Update? Should nonpublic entities be provided with a delayed effective date? If so, how long of a delay should be permitted and why? Are there specific amendments that would require more time to implement than others? If so, please identify which ones and explain why.

AIA Response: *The proposed disclosures would take a significant amount of time, money and effort to implement these amendments, all while providing little benefit or decision useful information to users. We have not expressed a view on an effective date because we believe that property and casualty insurers should be scoped out of the proposed disclosure requirement altogether. If, nevertheless, the FASB continues to believe some additional disclosure is needed, we recommend that any expanded disclosures for property and casualty insurers be deferred at this time and considered along with the Insurance Contracts project.*

Question 22: Do you believe that any of the amendments in this proposed Update provide information that overlaps with the SEC's current disclosure requirements for public companies without providing incremental information? If yes, please identify which proposed amendments you believe overlap and discuss whether you believe that the costs in implementing the potentially overlapping amendments outweigh their benefits? Please explain why.

AIA Response: *We believe the cash flow obligations table overlaps with the SEC's contractual obligations disclosures currently required in Management's Discussion and Analysis (MD&A). Due to the forward-looking nature of the estimates that would be required by the proposed disclosure, the MD&A section of the 10-K annual report filing is the appropriate area for making the requested disclosures, due to the protection provided under U.S. securities laws. As mentioned above, we do not believe there are any benefits to the Board's expanded disclosure proposals that would outweigh the increased operational costs and legal risks to produce them.*

Thank you again for the opportunity to respond to the proposed update. Please feel free to contact AIA with any questions or concerns.

Sincerely,

/s/ Phillip L. Carson

Phillip L. Carson
Associate General Counsel