

IASB Meeting October 2009 FASB Meeting

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Project Insurance Contracts

Topic Cover note

Agenda papers for this meeting

1. We have prepared the following agenda papers for the October meeting:

Agenda Paper No.	Title	Objective
4	Cover note	Outlines objectives for this meeting and next steps.
4A	Unbundling	Discusses whether to account for components of an insurance contract as if they were separate contracts.
4B	Presentation of the performance statement	Provides material for a preliminary discussion on the presentation of the performance statement.
4C	Deposit Floor	Discusses whether the measurement of an insurance liability should include a deposit floor.
4D	Timetable	Gives the time table for Board discussions.

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Objective of the meeting

- 2. An insurance contract may contain insurance, deposit (or financial) and service components. Agenda paper 4A discusses whether to account for those components of a contract as if they were separate contracts (unbundling).
- 3. The purpose of agenda paper 4B is to provide material for a preliminary discussion on the presentation of the statement of comprehensive income. This paper will also be re-used for a discussion on presentation at the October joint meeting. [Staff will prepare a separate paper for the October joint meeting that deals with measurement and acquisition costs].
- 4. In its May 2009 meeting, the IASB decided tentatively that the measurement of insurance contracts should include the expected cash flows resulting from those contracts, including those cash flows whose amount or timing depends on whether policyholders exercise options in the contracts. In staff's view, one consequence of that approach is that the measurement of insurance contracts can be less than the amount payable on demand (ie does not include a deposit floor). The purpose of paper 4C is to ask the IASB for confirmation of that consequence.
- 5. Agenda paper 4D includes the updated time table for Board discussions.

Tentative decisions to date

6. In previous meetings, the boards discussed a list of candidate measurement approaches for insurance liabilities. The appendix to this paper gives overview of the topics that were addressed.

Appendix: Overview of topics discussed at previous meetings

Topic	IASB	FASB
Candidate measurement approaches	The IASB tentatively selected the approach being developed in the project to amend IAS 37, modified to exclude day one gains.	The FASB tentatively selected a current fulfilment approach with a composite margin.
	Nevertheless, a significant minority of Board members supported the approach based on current fulfilment value. Therefore, the exposure draft will explain both approaches.	The FASB will consider at a future meeting whether an approach for measuring insurance contracts would include using future cash flows with no margins and no discounting in certain instances.
Features of a measurement approach	A measurement approach for insurance contracts conceptually should: (a) use current estimates of financial market variables that are as consistent as possible with observable market prices (b) use explicit current estimates of the expected cash flows (c) reflect the time value of money (d) include an explicit margin.	A measurement of the fulfilment value of an insurance contract should use expected cash flows rather than a best estimate of cash flows. Those expected cash flows should be updated each period. The measurement of cash flows should consider all available information that represents the fulfilment of the insurance contract. All available information includes, but is not limited to, industry data, historical data of an entity's costs, and market inputs when those inputs are relevant to the fulfilment of the contract. The measurement of cash flows should be discounted and the discount rate should be updated each reporting period. The FASB will continue to discuss at a future meeting what discount rate should be used.

Topic	IASB	FASB
Unearned	The IASB decided tentatively	The FASB will discuss an
Premium	that:	unearned premium approach at a
	(a) an unearned premium	future meeting.
	approach would provide	
	decision-useful information	
	about pre-claims liabilities	
	of short-duration insurance	
	contracts.	
	(b) to require rather than permit	
	the use of an unearned	
	premium approach for those liabilities.	
Measurement	The margin at inception should	In principle the initial recognition
of margins at	be measured by reference to the	of an insurance contract should
inception	premium. Therefore no day one	not result in the recognition of an
mooption	gains should be recognised in	accounting profit.
	profit or loss (except for the part	and a manage for a
	of the premium that covers	
	acquisition costs, as discussed	
	in more detail below).	
	If the initial measurement of an	The FASB will continue to
	insurance contract results in a	discuss this issue (day-one loss)
	day-one loss, the insurer should	at a future meeting.
	recognise that day-one loss in	
	profit or loss.	

Topic	IASB	FASB
Subsequent	On the residual margin, the	The FASB will discuss the
treatment of	IASB decided tentatively that:	subsequent treatment of margins
margins	a) the driver selected for	at a future meeting.
	releasing the residual	
	margins should result in	
	recognising those margins	
	in income in a systematic	
	way that best depicts the	
	insurer's performance under the contract.	
	b) that the residual margin	
	should be released over the	
	period during which the	
	insurer is standing ready to	
	accept valid claims (the	
	coverage period).	
	c) that the insurer should not	
	adjust the residual margin in	
	subsequent reporting	
	periods for changes in	
	estimates.	
Discount	The IASB decided tentatively	The FASB will discuss this issue
rates	that:	further at a future meeting.
	a) the discount rate for	S
	insurance liabilities should	
	conceptually adjust	
	estimated future cash flows	
	for the time value of money	
	in a way that captures the	
	characteristics of that	
	liability rather than using a	
	discount rate based on	
	expected returns on actual	
	assets backing those liabilities	
	b) the standard should not give	
	detailed guidance on how to	
	determine the discount rate	

Topic	IASB	FASB
Acquisition costs	The Board discussed an example in which two insurers issue identical insurance contracts but incurred different acquisition costs and, as a result, charged premiums that differ by the same amount. The Board decided tentatively that those contracts should have the same initial measurement.	 An entity: should expense all acquisition costs when incurred. should not recognize any revenue (or income) to offset those costs incurred.
	As a follow up, the Board decided tentatively that at inception an insurer should recognise as revenue the part of the premium that covers acquisition costs. For this purpose, acquisition costs should be limited to the incremental costs of issuing (ie selling, underwriting and initiating) an insurance contract and should not include other direct costs. Incremental costs are those costs that the insurer would not have incurred if it had not issued those contracts.	

Topic	IASB	FASB
Policyholder	The measurement should	The FASB will discuss this issue
behaviour	include the expected (ie	further at a future meeting.
and contract	probability-weighted) cash	
boundaries	flows (future premiums and	
	other cash flows resulting from	
	those premiums, eg benefits and	
	claims) resulting from those	
	contracts, including those cash	
	flows whose amount or timing	
	depends on whether	
	policyholders exercise options	
	in the contracts.	
	To identify the boundary	
	between existing contracts and	
	new contracts, the starting point	
	would be to consider whether	
	the insurer can cancel the	
	contract or change the pricing	
	or other terms. The staff will	
	develop more specific proposals	
	for identifying the boundary.	
Policyholder	The IASB decided tentatively	The FASB will discuss this issue
accounting	not to address policyholder	at a future meeting.
	accounting in the exposure	
	draft, but clarified that the	
	exposure draft should address	
	how both parties - the cedant	
	and the reinsurer - should	
	account for reinsurance	
	contracts.	