STAFF PAPER

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Project **Insurance Contracts**

Paper topic: Measurement of Contracts with Policyholder Participation: the Story so Far

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What is this paper about?

1. This paper reports to the IASB the decisions reached at the 30 November FASB meeting. It also provides background on the measurement of insurance contracts where the cash flows depend wholly or partly on the performance of other assets or liabilities of the insurer (or the performance of the insurer itself) using the decisions taken by both the IASB and the FASB so far. We do not ask the boards for a decision in this paper.

Structure of this paper

2. This paper is structured as follows:
    (a) Background, including the board's tentative decisions of the joint deliberations, a report on the FASB non-discretionary participating contracts' discussion and a discussion of participating features (paragraphs 3 - 11).
    (b) How the building block model could result in an accounting mismatch for performance-linked participating features (paragraphs 12 - 16).
    (c) How those accounting mismatches are eliminated through the boards' tentative decisions to date (paragraphs 17 - 33).

Background

Tentative decisions to date

3. The boards jointly discussed insurance contracts with performance-linked participation features during the 11 May 2011 meeting.

4. At that meeting, the IASB tentatively decided that an insurer should:

   (a) include in the measurement of the insurance contract liability cash flows that depend on the performance of underlying items on the basis used in the IFRS financial statements to measure those underlying items. Such items could be assets and liabilities, the performance of an underlying pool of insurance contracts or the performance of the entity. The staff would consider whether this approach creates a need for any specific disclosures.

   (b) reflect, using a current measurement basis, any asymmetric risk-sharing between the insurer and the policyholder in the contractually linked items arising from a minimum guarantee.

   (c) present changes in the insurance contract liability in the statement of comprehensive income consistently with the presentation of changes in the linked items (ie in profit or loss, or in other comprehensive income).

   (d) apply the measurement approach in (a)-(c) to both unit-linked and participating contracts.

   In addition, the IASB tentatively decided to proceed with the proposals in the IASB's exposure draft (ED) for consequential amendments relating to the following items held in unit-linked funds: financial instruments issued by the insurer (eg treasury shares) and owner-occupied property.

5. In part, because the FASB had tentatively reached separate conclusions, the FASB re-deliberated this topic during the 30 November meeting referred to above. Although the wording of the FASB and IASB tentative conclusions differ, the staff believe the tentative decisions regarding the measurement of the obligation from any performance-linked participating features that are in the scope of the boards' tentative decisions are substantially equivalent (i.e. it is based on the

measurement basis of the underlying items in the U.S. GAAP/IFRS statement of financial position).

Report on the FASB non-discretionary participating contracts' discussion

6. The FASB continued their discussion of the accounting for non-discretionary performance-linked participating features on 30 November 2011. This discussion and the tentative decisions reached were limited to the participating feature itself and were not intended to address embedded options and guarantees or other rights or obligations of the contracts. It is the staff's expectation that these remaining rights and obligations will be subject to either the overall insurance contracts standard or other applicable GAAP. That said, the measurement of the guarantees is the subject of Agenda Paper 7F/77F.
7. During the 30 November meeting, the FASB tentatively decided the following, as it relates to the measurement of insurance contract fulfilment cash flows, the measurement of the obligation from any non-discretionary performance-linked participating features that both contractually depend wholly or partly on the performance of other assets or liabilities recognized on the insurer's statement of financial position, or the performance of the insurer itself, and are a component of an insurance contract's obligations:

    (a) The obligation due to the performance-linked participating features should be measured based on an insurer's current liability (i.e., the contractual obligation incurred to date) adjusted to eliminate accounting mismatches that reflect timing differences between the current liability and the measurement of the underlying items in the U.S. GAAP/IFRS statement of financial position that are expected to reverse within the boundary of the insurance contract. An underlying item is defined as the asset or liability on which the cash flows resulting from the participation feature depend.

    (b) Any changes in the liability for the performance-linked participating feature should be presented in the same way within the statement of comprehensive income (i.e., consistently in net income and / or other comprehensive income) as the changes in the underlying item.

(c) No further adjustments beyond those described in (a) should be made to the performance-linked participating feature liability measurement for the purposes of reflecting expected cash flows.

8. This paper provides an overview of these decisions and considers how they would apply in practice.

Participation features

9. For some insurance contracts, some or all of the cash flows depend wholly or partly on the performance of other assets or liabilities of the insurer. Such dependence may take a variety of forms, including:

   (a) A direct pass-through of all the returns from a specified pool of assets (as in unit-linked or variable contracts).

   (b) A direct pass-through of all the returns from a specified pool of assets, combined with a guarantee of a minimum return. We discuss the accounting for such guarantees in Agenda Paper 7F/77F.

   (c) A direct contractual link that gives the policyholder the right to receive a share of the performance of the insurer or a segregated fund, expressed in terms of a percentage (eg 90%) of the annual surplus achieved under a specified accounting basis. In most cases that basis would differ from IFRS and US GAAP. Although contracts vary in details from jurisdiction to jurisdiction, the approach of specifying a link through a percentage of surplus is very common in many countries throughout the world.

   (d) Contracts that have a link to surplus, but lack a specified minimum percentage or for which the specified minimum percentage is 0%. These are common in Belgium and some states of the USA.

   (e) An account balance driven contract with variable annual credits and charges to the policyholder's account balance that depend on the overall performance of the insurer (such as ordinary universal life contracts[1]). These often include a minimum crediting rate but, are purchased by policyholders under the assumption that the insurer will credit their account with an additional return, the amount of which is left to the insurer's discretion.

Terms and definition

10. The term '**participation**' is often used to refer to different types of products. The discussion of participation sometimes lacks clarity because the term is not defined and people often associate it only with the products issued in their own regulatory environment. Appendix A provides further background on participating contracts and Appendix B gives an international overview of the different types of contracts.
11. For ease of reference, this paper uses the following terms:

    (a) The **underlying items** or the **underlying assets or liabilities** are the assets or liabilities on which the cash flows resulting from the participation feature depend. Depending on the circumstances, the underlying assets or liabilities may be investments held by the insurer, liabilities of the insurer, a pool of insurance contracts of the insurer or even the entire performance of the insurer. To simplify the discussion, the rest of this paper deals mainly with underlying assets that are investments, but in general similar principles would apply to other underlying assets or underlying liabilities.

    (b) The **performance-linked participation feature** is the contractual feature that creates the link between the performance of the underlying assets or underlying liabilities and the resulting cash flows to policyholders. The

[1] A permanent life insurance policy with terms that are not fixed or guaranteed with respect to premium amounts, expense assessments, or benefits accruing to the contract holder. The policy contains a savings element that is invested to provide a cash value accumulation. The death benefit, savings element, and premiums can be reviewed and altered as the policyholder's circumstances change within certain limits stated in the policy. The cash value grows at a variable rate that is adjusted monthly (sometimes it is pegged to a financial index such as a stock, bond or other interest rate index). The policyholder may use the interest from the accumulated savings to help pay premiums. This policy divides the pure insurance protection, the related expense charge, and the cash value accumulation into separate and distinct components.

contractual feature may result from explicit terms in the contract, or from related legal or regulatory requirements.

(c) The **performance-linked cash flows** are the cash flows to the policyholder that result from the performance-linked participation feature. The main issue this paper deals with is how to include these cash flows in the measurement of the insurance liability.

(d) The **statutory accounting basis**[2] is the basis described in an insurance contract for determining the amounts currently available for distribution.

How the building block approach could result in an accounting mismatch for performance-linked participation features

12. This section describes how the treatment of performance-linked participation features in the building block approach proposed in the ED can give rise to accounting mismatches.

13. In some respects, the result obtained by applying the building block approach to the insurance contract liability can be viewed as broadly similar to fair value. Both fair value and the building block approach measure contracts by discounting the expected cash flows at a current market-consistent discount rate. However, there are some differences between fair value and the measurement under the building block approach, namely:

(a) The insurance contracts measurement approach uses entity specific assumptions for some inputs, including the degree of risk aversion. Fair value uses market participant assumptions.

(b) The insurance contracts measurement approach excludes the insurer's own non-performance risk. Fair value would include own non-performance risk.

[2] The staff is aware that the basis may not necessarily be a statutory basis in each case. However, the staff believe that this term eases the discussion because in many cases it will be a statutory basis and people often refer to the 'statutory accounting' as being relevant for the participation.

(c) The insurance contracts measurement approach, as tentatively decided by the FASB, does not remeasure the risk adjustment (which, is implicitly included in fair value) but instead includes it implicitly at inception in the single margin which is later run off based on the release of risk.

14. Consequently, if all the underlying assets (or liabilities) are measured at fair value through profit and loss in the financial statements and the insurance liability is measured under the building block approach, limited accounting mismatch arises (ie only those arising from the differences identified in paragraph 13). This is discussed in paragraphs 20-27.

15. However, in many cases the underlying asset/liabilities are not carried at fair value through profit and loss in the IFRS/ US GAAP financial statements. Consequently, an accounting mismatch will arise. This is described in paragraphs 29-33. The following simplified example illustrates how such an accounting mismatch arises.

Example

Background

Assume there is an asset with a fair value of CU1,200. The IFRS/US GAAP carrying amount is CU1,000. The policyholder receives CU1,000 and 90% of the performance of this asset above CU1,000. Assume that the fair value of the guarantee that the policyholder will receive at least CU1,000 is CU5.

Application

Under the proposals in the ED/DP, the insurance contract liability would be measured at CU1,185 because it would include the following:

- CU1,000

- 90% of the CU200 =CU180 (Fair Value above carrying amount, ie CU1,200 – CU1,000)

- CU5 (the value of the guarantee)

16. In this case, there is an accounting mismatch of CU180 for the remaining difference between the IFRS/US GAAP carrying amount of the assets of CU1,000 and the expected present value of the cash flows of the insurance contract liability of CU1,185. The fair value of the guarantee of CU5represents an economic

mismatch. In other words, measuring all future performance-linked cash flows on a different basis from the underlying item creates an accounting mismatch.

How the accounting mismatches are eliminated through the board's tentative decisions to date

17. This section discusses how accounting mismatches arising from the building block approach described in paragraphs 12-16 are eliminated through the boards' tentative decisions, both in measurement and in presentation.
18. The discussion is separated in two cases:
    (a) When the assets are carried at fair value through profit or loss in IFRS/US GAAP and another basis under statutory
    (b) When the assets in IFRS/US GAAP are carried at the same basis as under statutory.
19. Staff did not analyse the situation where IFRS/US GAAP measurement is neither fair value nor statutory as this is a hybrid of the two base cases discussed here.

When underlying assets are carried at fair value through profit or loss

Starting from the building block approach

20. In the first case we assume that the underlying assets (or liabilities) are measured at fair value through profit and loss in the financial statements, and the performance-linked payments to policyholders depend on changes in the value of underlying assets (or liabilities) that are determined on a different basis. (In many jurisdictions, the basis applied to the underlying assets (or liability) to determine amounts available for distribution to policyholders is a cost basis, with the policyholders participating in realised gains and losses only).
21. However, because the carrying amounts of the underlying assets used in the financial statements (e.g., fair value) and the amounts used to determine performance-linked payments for the current period (eg statutory accounting) can be different, there may be a timing difference between the timing of changes in fair value and the time when the performance-linked payments are determined.

Those timing differences are analogous to the temporary differences used in accounting for deferred taxes.

22. Nonetheless, the building block approach would in effect measure the insurance contract liability on a basis that reflects the fair value of the underlying assets (and liabilities) and thus substantially eliminate those timing differences, even when the amount currently available for distribution is determined on a cost basis. Thus, no adjustment is needed in the building block approach to deal with these cases.
23. However, staff note that some respondents overlooked this implication of the treatment in the ED/DP. The staff will consider in drafting how to clarify this point to readers.

Starting from the statutory accounting basis

24. While the IASB based the measurement of performance linked participating contracts on a basis that starts with the approach proposed in the ED for all insurance contracts, the FASB's discussion took another starting point, the liability incurred-to-date determined on a statutory accounting basis. The fact that the insurer's 'incurred-to-date' liability is calculated on a statutory basis can result in timing differences between the measurement of the underlying assets in the financial statements and the measurement of the 'incurred-to-date' liability. However, regardless of how the underlying items are measured in the financial statements, the ultimate payments under the contracts will be the same (to the extent the timing difference reverses within the boundary of the insurance contract). To avoid creating an accounting mismatch, the FASB decided that the measurement of the insurance contract liability should be adjusted to eliminate any such timing differences when that obligation is reported in the US GAAP financial statements.
25. This is similar to accounting for deferred taxes where the tax basis balances are compared with the IFRS/US GAAP-basis to identify the temporary differences.
26. Although some argue that adjustment of the measurement of the underlying item would eliminate the timing difference between statutory and IFRS/US GAAP, the FASB concluded that adjusting the liability would be a better reflection of the linkage between the underlying item and the performance-linked participating

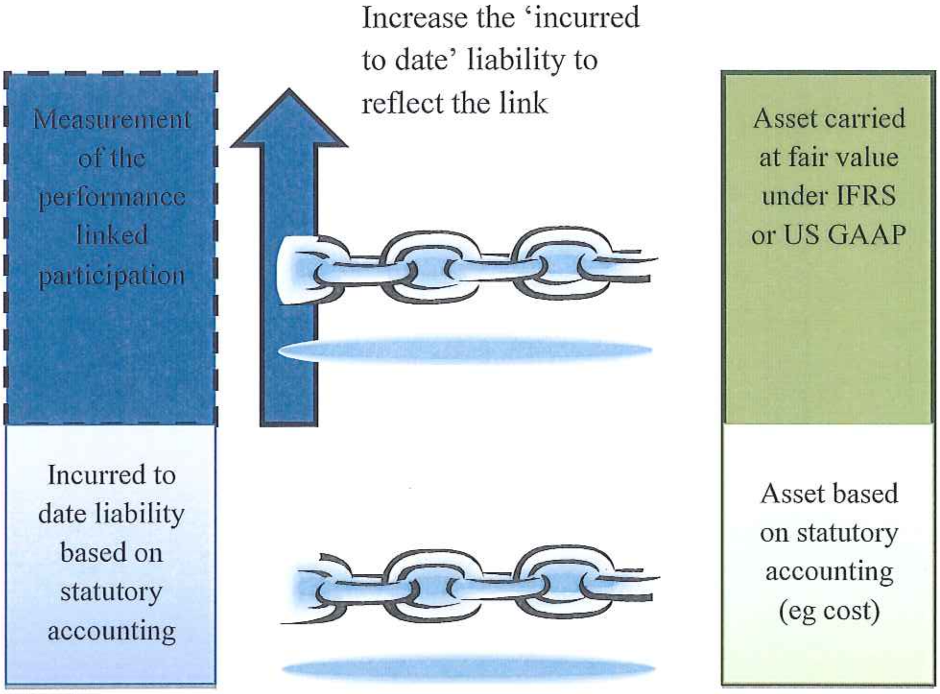
feature. The FASB's rationale for this conclusion is that it believes adjusting the insurance contract liability, rather than the underlying asset would:

(a) reflect the reasons why those underlying items are measured on the basis required by the respective standards;

(b) neither require different accounting for two identical assets held by an insurer nor measure all of the insurer's assets in a manner that might reduce comparability with other entities. For example, if the insurer held an asset measured using cost and, policyholders participated only in, say 10% of the increase in fair value of the asset, with the insurer keeping the remaining 90%, it would reduce comparability with other assets held at cost to require the insurer to measure the underlying asset at fair value.; and

(c) neither require application of the insurance contract measurement model to assets it was not designed to measure nor result in introducing additional accounting mismatches (e.g. for any portion of the underlying items that don't pass through to the policyholder) that would arise if the underlying items were required to be measured on whatever basis is used to measure the performance-linked contractual feature.

27. The following diagram illustrates how the change in the measurement attribute for the asset between the statutory basis (eg a cost basis) to fair value would be reflected by the FASB tentative decision:



When underlying assets are not carried at fair value through profit and loss

28. In this section, we discuss the implications if the assets are not carried at fair value. As discussed in paragraph 19, we assume that in this case the IFRS / US GAAP basis is the same as the statutory basis. If that is not the case, ie if the underlying assets are carried at value that is neither fair value nor the statutory basis, there would be an adjustment to the building block as well as adjustment from the statutory measurement basis. The mechanics would be a combination of the adjustments in described in paragraph 20 - 27 and the ones described in this section. Therefore the staff has not included these adjustments in the analysis.

Starting from the building block approach

29. As illustrated in the example, an accounting mismatch will arise between the insurance contract liability and the underlying items when the underlying items are **not** measured at fair value through profit and loss in the financial statements and the performance-linked participating feature is measured based on the building block approach (i.e. similar to fair value). There are two ways to avoid this accounting mismatch:

(a) the measurement of the underlying items could be adjusted so that they are measured at fair value through profit or loss (although a mismatch may still arise from the differences identified in paragraphs 14 - 15), or

(b) the measurement of the insurance contract liability could be adjusted to reflect the measurement basis of the underlying items.

30. In May 2011, the IASB concluded that an insurer should **not** measure **all** underlying items at fair value to avoid such a mismatch for the following reasons:

(a) Many participating contracts are linked to the performance of items such as goodwill in subsidiaries, deferred tax assets, pension liabilities, owner-occupied property and other assets or liabilities, many of which only a portion of the change in value will accrue to the policyholder.

(b) Requiring fair value measurement for underlying items would not provide relevant and comparable information to users of financial statements. If one industry is required to use fair value for assets and liabilities that are normally measured on a different basis, comparability would be reduced.

(c) Because the liability is the result of payments that result from the performance of the underlying items, some regard it as more intuitive to adjust the liability, rather than the underlying items.

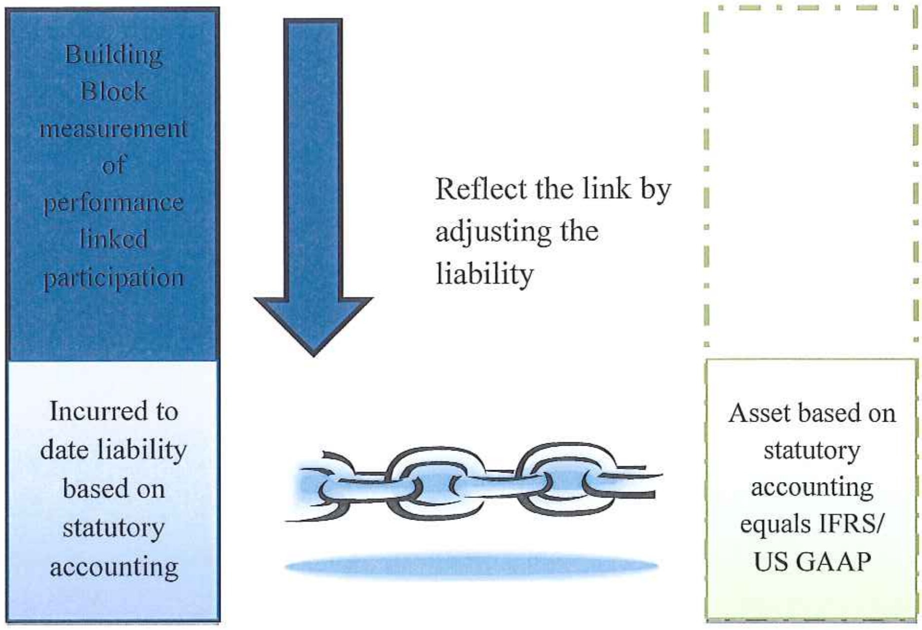
31. The boards also did also **not** require that insurers should **use existing fair value** options to eliminate the accounting mismatch, because:

(a) Requiring insurers to apply the fair value option to eliminate the mismatch does not consider the reasons why the accounting standards provide different measurement attributes.

(b) Most participating contracts share the performance in at least some assets or liabilities that do not provide a fair value option. Applying existing fair value options supplemented by a 'mirroring approach' for all other underlying items would not achieve the goal of a market consistent measurement of the overall liability, because they would not eliminate all of the accounting mismatch and would instead result in only a patchwork solution.

32. Thus the IASB concluded that the best way to eliminate the accounting mismatch would be to require insurers to adjust the measurement of the insurance contract liability to reflect the measurement of the underlying item.

33. The following diagram illustrates the IASB decision on how to adjust the building block liability, if the assets are carried on the same basis for IFRS / US GAAP and statutory. It should be noted that if the carrying amount of the asset is neither the statutory value nor the fair value, both IASB and FASB would adjust the liability.



Starting from the statutory accounting basis

34. If the insurance contract liability is measured starting from a statutory accounting basis, then no mismatch arises because the insurance contract liability would not be measured at fair value assuming that the assets were also measured on the basis of that statutory accounting. Therefore no adjustment would be needed to deal with these cases.

Presentation

35. Although the measurement mismatch might be eliminated, there might be a presentation mismatch to consider. Based on the tentative decisions of the boards, any changes in the liability for the performance-linked participating feature should

be presented in the statement of comprehensive income consistently with changes in the underlying item (i.e. in profit or loss, or in other comprehensive income). Thus, when changes in the underlying assets are presented in other comprehensive income, the related changes in the insurance contract liability would also need to be presented in other comprehensive income to avoid a presentation mismatch.

Summary

36. Although the wording differs, both the IASB and FASB tentatively decided to adjust the measurement of the obligations that depend on underlying items in a way that reflects how those underlying items are measured in the financial statement. That is achieved either by:
    (a) eliminating from the building block approach changes in value not reflected in the measurement of the underlying items, or
    (b) including in the statutory liability changes in value that are reflected in the measurement of the underlying items.

Appendix A: History of policyholder participation

A1. The best way to understand policyholder participation is to have a look at the history of insurance and how participation features in insurance contracts have developed. Insurance developed based on the fact that there are unfavorable events which are too severe for one person to face the financial impact.

> The first methods of transferring or distributing risk were practiced by ancient traders. When travelling treacherous river rapids they would redistribute their wares across many vessels to limit the loss due to any single vessel's capsizing.

A2. It is important to keep the concept of distributing the risk among a pool of people in mind when one tries to understand policyholder participation. When insurance became more sophisticated than the example above, people paid a premium (an estimated share in the overall loss of the pool plus a margin for the risk of unfavorable developments) in advance. The total premiums of the pool were used to pay the losses. Any remaining surplus was re-distributed to the participants of the pool. This can be seen as the first participation feature, **linking** the re-payment of parts of the premium to the **performance** of the pool.

A3. The pool would also use the funds provided by its members and invest them until the losses had to be paid. These **investment results** and all the **costs** of the pool were also taken into consideration, when the surplus was distributed.

A4. The pools later developed into mutual insurers, owned by the policyholders. As a next step, these mutual insurers, as subsequent stock companies generally, started to guarantee minimum benefits or maximum premiums. While the entire surplus in the earlier pools had been distributed after the period, these insurers would need additional capital for events where the loss of the year would exceed the agreed upon premium. This need for additional capital was addressed by charging increased premiums, some of which was refunded if the loss experience was better than anticipated in the determination of the premium (participation is often as well referred to as premium refund).

A5. Participation features later became more sophisticated, specifically the contractual or legal regulation of the split between insurer and policyholders, and some are meanwhile only loosely linked to the concepts above. An important distinctive difference between participation systems is, whether the obligations of the insurer are collective or whether individual policyholders have a direct right to receive shares of current surplus from their contracts. In the collective case, some parts of today's surplus might be distributed to future policyholders since the obligation to current policyholders requires only that those amounts are distributed to any policyholder rather than requiring distribution to the current policyholders.

Appendix B: Summary background paper from May

The following is an extract from the May 2011 topic overview on participation features.

Geographical variations in participation features

B1. This section of the appendix is carried forward from Appendix B for agenda paper 3F/ FASB Memorandum 60F of the May 2011 Joint Board meeting. It should remind the boards of the variety and complexity of participating contracts in practice.

B2. In most countries the insurer's discretion is at least partially constrained by legal or regulatory requirements as well as by competitive constraints. In many countries the "contribution principle" applies. The contribution principle means that the distribution of the aggregate accumulated surplus among the policyholders is in the same proportion as each respective contract (or portfolio of contracts) that has contributed to the accumulated surplus.

B3. The following information on country-specific types of participating contracts is based on an (internal) survey by members of the Insurance Accounting Committee of the International Actuarial Association (IAA). We thank them for providing the information. They are not responsible for the way in which the IASB staff have summarised the information.

B4. **Belgian** participating contracts provide a contractual right to share in surplus, but usually do not give specific guidance on how the policyholder participates in the surplus or which share belongs to the policyholder. The insurer determines annually the policyholders' share of surplus, which is solely based on the insurer's discretion (the insurer is entirely free to pay the policyholder any amount between 0 to 100% of the surplus). After determining the policyholders' share in surplus for the current year, the Belgian regulators require the insurer to pay out 80% of the amounts set aside for allocation to policyholders in the following year. The remaining 20% are to be payable to policyholders in later periods.

B5. **Finnish** participating contracts determine the policyholders' share entirely based on the insurer's discretion. The insurer decides when to realise surpluses, the individual policyholder's share in that surplus and the timing of the actual allocation. The Insurance Company Act contains a prescription on policyholder participation, Principle of Fairness, which is understood to mean that a reasonable part of surplus must be returned to the policyholders. The insurer is obliged to publish its bonus target in its website and in the annual accounts. In the annual accounts the insurer must assess how the target has been complied and the possible reasons for non-compliance. The regulator ensures that the insurer does not allocate surpluses if doing so potentially endangers the insurer's financial stability.

B6. **French** life insurers issue participating investment contracts with a guaranteed minimum annual rate of return on premiums paid, a distinct share in investment returns on the entire surplus of the entity. Under French law the insurer can immediately forward shares in realised surplus to individual policyholders. The remaining amount of the overall required share for policyholders is set aside. However, the insurer has some discretion regarding the timing of the allocation to the individual policyholder. The allocation has to be done within 8 years. The amount set aside can be used to cover subsequent losses to some extent and there might be as well a loss carry forward to be recovered by future surplus.

B7. **South African** life insurers have discretion on the policyholders' share in surplus, as well as on the amount and timing of its allocation or distribution to the individual policyholder. The amounts set aside for policyholders can be negative if they are expected to be recovered during the following three years.

B8. In **Germany** virtually all life insurance contracts are participating contracts. There are strict rules determining the share of recognised surplus that has to be set aside for participation of policyholders. Although the subsequent allocation of the amount set aside to individual policyholders is at the discretion of the insurer, the contribution principle is applied. Losses of a period are generally borne by the insurer. Unallocated amounts can be used to cover subsequent losses if otherwise the insurer would be in financial danger. If contracts terminate for any reason, the policyholder receives an appropriate share of unrealised gains allocable to its contract.

B9. In **Italy**, the participation feature is guaranteed by law to be an entity-wide average of 85% of the realised surpluses (unrealised gains and losses excluded). The exact policyholder's share in the surplus is specified in the individual contract as a specific percentage of investment earnings. The individual policyholder receives its share every year according to the results of the previous year.

B10. **Canadian** participating contracts require an annual allocation of amounts to individual policyholders, payable immediately in the following year. Law requires that the directors must adopt a formal dividend policy and adopt methods for allocation, which an appointed actuary must approve. In Canada there is little discretion in determining the amount or timing of the surplus once allocated. The contribution principle is followed, with the Appointed Actuary recommending dividends to the entity's Board.

B11. In **Australia** the policyholders' share in surplus is set aside and allocated to the individual policyholder according to a formula. Legally, the insurer is obliged to set aside 80% of the surplus for policyholders. Some contracts grant an even higher percentage. The amount set aside may become negative and carried forward. If the insurer voluntarily pays more than 80% (or whatever contractually is required), that can be carried forward, thus reducing future amounts to be set aside to pay dividends to future policyholders

B12. Most **Japanese** participating contracts force the insurer to immediately set aside policyholders' contractually specified share in the realised surplus. These amounts are not immediately payable to the individual policyholder, but rather are aggregated over time. The timing of the irrevocable allocation is at the discretion of the insurer, even though the surplus is already realised. The amounts set aside are revocable and loss absorbing, including those referring to future periods of the individual contract.

B13. In the **US**, the types of contracts are diverse, partly due to significantly different state regulations. Some states allow insurers to apply significant discretion in declaring dividend scales; however, overall they are subject to regulatory control. Regulators are expected to intervene in case of inadequate dividend scales, but that remains untested since in the past all insurers acted in accordance with regulatory rules. If stock insurers issue participating contracts, the amounts distributable to stockholders may be limited by some state laws.

B14. In some states in the US, e.g. New York, state law requires that the insurer sets a minimum percentage of surplus aside for ultimate distribution to policyholders each year. At the same time the law grants insurers some discretion regarding its ultimate allocation. The contribution principle is considered in this allocation.

B15. In the **UK**, participating features are contractually and legally established. The sources to determine the surplus need to be specified and may include sources from non-participating contracts. Policyholders' individual share is typically required to be at least nine times of any allocation to shareholders from aggregated unallocated surplus, to be allocated immediately to policyholders when amounts are allocated to shareholders.

B16. In the **Czech Republic** and **Slovakia**, participating contracts determine the policyholder's share as a fixed percentage of the realised surplus. The insurer's only discretion is when to realise the surplus, as there is no discretion on timing of allocation or amount of payment to the individual policyholder.

B17. **Norwegian** law prescribes that the policyholders' share in surpluses has to be two thirds of each annual surplus (partly including unrealised gains). When policies terminate, there is an obligatory payment of 75% of any surpluses (including unrealised gains) determined at that point in time. Insurers can decide when to realise gains (apart from terminating contracts), but there is no further discretion available.