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Project	**Insurance contracts**		
Paper topic	Whether to unlock the contractual service margin for changes in the risk adjustment		
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Objective

1. This paper considers whether to adjust the contractual service margin for changes in the risk adjustment. This is a follow-on issue that assumes that the IASB confirms the proposals in the IASB's 2013 Exposure Draft *Insurance Contracts* (the 'ED') to adjust (ie unlock) the margin for differences between current and previous estimates of the present value of cash flows relating to future coverage or other services as recommended in Agenda Paper 2A.

2. This paper is structured as follows:

   (a) the staff recommendations (paragraphs 3–4);

   (b) background on the proposals in the ED to recognise all changes in the risk adjustment in profit or loss (paragraphs 5–7) and relevant paragraphs from the Basis for Conclusions explaining the rationale behind the IASB's decision to recognise changes in the risk adjustment in profit or loss instead of recognising those changes by unlocking the contractual service margin (Appendix A);

   (c) summary of feedback received on the ED's proposal (paragraphs 9–14);

   (d) an analysis that considers whether changes in the risk adjustment should unlock the margin (paragraphs 15–20); and

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(e) a cost-benefit discussion for including an explicit risk adjustment in the measurement of the liability if the IASB accepts the staff recommendation (Appendix B).

Recommendations

3. The staff recommend that differences in the current and previous estimates of the risk adjustment that relate to coverage and other services for future periods should adjust the contractual service margin subject to the condition that the margin should not be negative. Consequently, changes in the risk adjustment that relate to the coverage and others services provided in the current and past periods should be recognised in profit or loss.

4. After the IASB has considered the treatment of the contractual service margin for participating contracts, staff will consider the tentative decisions together to see if the tentative decisions reached for non-participating contracts should be revisited, or vice versa.

The ED

5. The ED proposed to recognise changes in the risk adjustment in profit or loss instead of unlocking those changes in the contractual service margin.

6. In developing the ED, the IASB concluded that most of the change in the risk adjustment would relate to the expiry of risk in a period, and that it would be difficult to divide the risk adjustment into a part relating to a future period's coverage and a part relating to past and current periods' coverage. The IASB also observed that it would be more transparent to report changes in risk relating to expected changes in circumstances in profit or loss, and that changes in risk do not affect the amount of cash outflow, because the risk adjustment unwinds over time. Appendix A provides the relevant paragraphs from the Basis for Conclusions that explain the rationale behind the IASB's decision to recognise changes in the risk adjustment in profit or loss instead of recognising those changes by unlocking the contractual service margin.

7. The IASB's proposal to recognise all changes in the risk adjustment in profit or loss creates an inconsistency between how the margin is determined at inception and subsequently. At inception, the margin is the residual difference between the (a) cash inflows and (b) the cash outflows plus risk adjustment. Subsequently, the risk margin does not affect the amount recognised as the contractual service margin.

8. Subsequently, the recognition of changes in the risk adjustment in profit or loss is consistent with the following proposals to recognise subsequent changes of the following estimates in the statement of comprehensive income rather than through the margin:

   (a) the effects of changes in discount rates. The effects of changes in discount rates are recognised in the statement of comprehensive income because they reduce accounting mismatches with the assets that back those contracts (see Agenda Papers 2D and 2E).[1]

   (b) for reinsurance assets held by the cedant. Changes in the credit risk of the reinsurer are recognised in profit or loss because they do not relate to the provision of services.

   (c) for contracts that require the entity to hold underlying items and specify a link to returns on those underlying items, changes in the options and guarantees are recognised in profit or loss. This provides more transparent information on the current value of these options and guarantees.

Summary of feedback received

9. A few respondents supported the IASB's proposals to recognise changes in the risk adjustment in profit or loss because:

[1] The staff note that some comment letters suggested that changes in discount rates should also unlock the margin, to be consistent with the fact that they were included in the margin on initial recognition. Because Agenda paper 2D recommends that the Board confirm the proposals in the ED to present the effect of change in discount rate in OCI, the staff do not propose to explore that suggestion further.

(a) they believe that it would be arbitrary to split changes in the risk adjustment for changes relating to future and past/current coverage.

(b) they view the changes in the risk adjustment as analogous to changes in assets and liabilities recognised at fair value through profit or loss. They note that one of the reasons for an explicit risk adjustment in the measurement of an insurance contracts liability is that it is consistent with fair value measurement. Fair value measurement would factor in the degree risk associated with the item.

(c) they note that changes in the risk adjustment can be significantly affected by changes in the discount rates. Consequently, they would prefer that changes in the risk adjustment be recognised in the statement of comprehensive income consistently with the effects of discount rate changes and the unwind of the discount rate.

10. However, most constituents believe that the correct approach would be to adjust the contractual service margin by changes in the risk adjustment that relate to future coverage, and to report the change in the risk adjustment relating to current and past coverage in profit or loss. Under the ED, the risk adjustment depicts the compensation that the entity requires for bearing the uncertainty that is inherent in the cash flows that arise as the entity fulfils the portfolio of insurance contracts. Of these constituents some see the risk margin and the contractual margin as interdependent because the risk adjustment reflects the compensation required for bearing the variability inherent in the cash flows and the contractual service margin is determined as the difference between those cash inflows and cash outflows. Some note that unlocking the margin for changes in the risk adjustment is consistent with the measurement of the margin of day one (ie the margin is the difference between the premiums and the expected present value of the cash outflows plus the risk adjustment).

11. In addition, some noted that the same arguments for unlocking the margin for changes in estimates of cash flows also applies to unlocking the margin for changes in the risk margin:

(a) some are concerned that recognising changes in risk adjustment in profit or loss could result in losses being recognised in profit or loss in one period even if the contract overall is profitable.

(b) some view the contractual service margin as a 'cushion' for the volatility arising in changes in assumptions. Those who hold this view would also unlock the margin for changes in the risk adjustment.

(c) some think that the proposal in the ED to recognise all changes in the risk adjustment in profit or loss may allow more room for management manipulation of amounts in profit or loss. While they support an explicit risk adjustment, they note that the determination of the risk adjustment is highly subjective because it is affected by the entity's assessment of the price of risk.

12. Furthermore, some constituents challenged the IASB's assumption that the main driver of the change in risk adjustment would be expected to be related to the expiry of coverage (see paragraph 5). They note that changes in cash flows to be paid out in future can have a material impact on the risk adjustment. Accordingly, they believe that adjusting the contractual service margin for changes in the risk adjustment relating to future service would provide better information for users of financial statements.

Complexity

13. Adjusting the contractual service margin for changes in the risk adjustment relating to coverage or other services that are to be provided in future periods will increase complexity. As noted in paragraph 5, entities would need to decompose changes in the risk adjustment into:

(a) changes relating to current and past coverage (ie the release from risk during the period and the changes in risk relating to claims incurred in past or current periods); and

(b) changes in risk relating to coverage provided in future periods.

Changes in the risk adjustment relating to (a) would be recognised in profit or loss and changes relating to (b) would adjust the margin.

14. Views are mixed on the feasibility of dividing the risk adjustment in this way:

    (a) the majority of constituents, particularly those in Europe, Australia and North America, state that it is relatively straightforward to separate the risk adjustment between the part related to future coverage and the part related to current and past coverage. They state that existing methods for determining the risk adjustment already make this information available. For example, regulatory reporting for general insurance in Australia already requires a similar separation.

    (b) a few think that it would not be feasible, or that the costs would outweigh the benefits, to divide the risk adjustment into a part relating to future service and a part relating to current and previous years' service, particularly because the IASB has not mandated a particular method for determining the risk adjustment. They also question whether the effect would be material. Some suggest that taking the whole of the change in the risk adjustment to profit or loss, as proposed in the ED, is a more practical approach.

Analysis

15. The staff note that there are mixed views on what the margin represents, which results in differences in views on whether the risk adjustment should be recognised in profit or loss or adjusted through the margin (as discussed in paragraphs 9–11).

16. On balance, the staff think that unlocking the contractual service margin for changes in the risk adjustment relating to coverage or other services that are to be provided in future periods would increase consistency of the margin determined at inception and on day two—that the margin is the risk-adjusted profit for the contract to be earned as the coverage or services are provided in the future. While unlocking the margin for changes in the risk margin increases consistency between the margin on day one and subsequently, the staff note that differences remain between the margin on day one and subsequently on three aspects under the proposals in the ED as detailed in paragraph 7.

17. The staff were also persuaded that the differences in current and previous estimates of the risk adjustment should be treated consistently with the changes in the current and previous estimates of the present value of cash flows to which the risk adjustment relates, because the risk adjustment is a measure of the variability of the present value of cash flows. This means that:

    (a) the contractual service margin should be unlocked for changes in the risk adjustment relating to coverage and other services provided in future periods, subject to the condition that the margin should not be negative.

    (b) changes in the risk adjustment relating to coverage and other services provided in the current or past periods should be recognised in profit or loss. For example, the release of risk relating to current periods and changes in the risk adjustment relating to claims incurred in past or current periods.

18. Finally, feedback indicates that decomposing the risk adjustment as described in paragraph 17 is operational (see paragraph 14(a)). Moreover, the majority of respondents believe that the benefits of adjusting the margin for changes in the risk adjustment relating to coverage and other services to be provided in future periods outweigh the costs of doing so.

Question for the IASB

Unlocking the margin for changes in the risk adjustment
Does the IASB agree that differences in the current and previous estimates of the risk adjustment that relate to coverage and other services for future periods should adjust the contractual service margin subject to the condition that the margin should not be negative? Consequently, changes in the risk adjustment that relate to the coverage and others services provided in the current and past periods should be recognised in profit or loss.

Cost-benefit analysis of determining an explicit risk adjustment in the light of the staff recommendation

19. The staff's recommendation has the consequence that changes in an explicit risk adjustment would have no effect in profit or loss or the statement of financial position to the extent that such changes adjust the contractual service margin.

20. Some question whether that consequence would alter the IASB's previous assessment that the benefits of the information provided by an explicit risk adjustment would outweigh the costs of determining it. However, as discussed in Appendix B, the staff believe that the benefits of an explicit risk adjustment continue to outweigh the costs of determining it, because the risk adjustment will continue to provide useful information through the disclosures and will have an effect on profit or loss and the statement of comprehensive income in circumstances in which the information is most relevant. The staff notes that most constituents that support an explicit risk adjustment also recommend unlocking the margin for some changes in the risk adjustment.

Appendix A: Extracts from the basis for conclusions of the ED

A1. The ED did not explicitly ask constituents for their comments on whether an explicit risk adjustment should be included in the measurement of the liability. The IASB consulted on this question twice previously in the 2007 Discussion Paper *Preliminary Views on Insurance Contracts* and the 2010 Exposure Draft *Insurance Contracts*.

A2. The following are relevant extracts from the Basis for Conclusions on why the IASB concluded on an explicit risk adjustment:

Reasons for including a risk adjustment in the measurement of an insurance contract

BCA92 This Exposure Draft proposes that the risk adjustment should depict the compensation that the entity requires for bearing the uncertainty that is inherent in the cash flows that arise as the entity fulfils the portfolio of insurance contracts.

BCA93 In developing the objective of the risk adjustment, the IASB concluded that a risk adjustment should not represent:

(a) the compensation that a market participant would require for bearing the risk that is associated with the contract. As noted in paragraph BCA19, the measurement model is not intended to measure the current exit value or fair value, which reflects the transfer of the liability to a market participant. Consequently, the risk adjustment should not be determined as the amount of compensation that a market participant would require.

(b) an amount that would provide a high degree of certainty that the entity would be able to fulfil the contract. Although such an amount might be appropriate for some regulatory purposes, it is not compatible with the IASB's objective of providing information that will help users of financial statements make economic decisions.

(c) a shock absorber for the unexpected or to enhance the entity's solvency.

BCA94 Some, including the FASB, oppose the inclusion of a risk adjustment in the fulfilment cash flows because:

(a) no well-defined approach exists for developing risk adjustments that would meet the objective and provide consistency and comparability of results.

(b) some techniques are difficult to explain to users of financial statements and, for some techniques, it may be difficult to provide clear disclosures that would give users of financial statements an insight into the measure of the risk adjustment that results from the technique.

(c) although practitioners may, in time, develop tools that help them to assess whether the amount of a risk adjustment is appropriate for a

given fact pattern, it is not possible to perform direct back-tests to assess retrospectively whether a particular adjustment was reasonable. Over time, an entity may be able to assess whether subsequent outcomes are in line with its previous estimates of probability distributions. However, it would be difficult, and perhaps impossible, to assess whether, for example, a decision to set a confidence level at a particular percentile was appropriate.

(d) developing systems to determine risk adjustments will involve cost, and some doubt that the benefits will be sufficient to justify that cost.

(e) the inclusion of an explicitly measured risk adjustment in identifying a loss at initial recognition is inconsistent with the IASB's 2011 Exposure Draft *Revenue from Contracts with Customers*.

(f) if the remeasurement of the risk adjustment for an existing portfolio of contracts results in a loss, that loss will reverse in later periods as the entity is released from that risk. Reporting a loss that is followed by an inevitable reversal of that loss may confuse some users of financial statements.

(g) they believe that, while the risk adjustment is a relevant concept for determining solvency, it risks introducing bias into the measurement of an insurance contract.

BCA95 However, the IASB proposes to require a separate risk adjustment because it believes that this:

(a) will result in an explicit measurement of risk that will provide a clearer insight into the core feature of insurance contracts. It will convey useful information to users of financial statements about the entity's view of the economic burden imposed on it by the presence of the risk associated with the entity's insurance contracts.

(b) will result in a profit recognition pattern that reflects both the profit that is recognised by bearing risk and the profit that is recognised by providing coverage and other services. As a result, the profit recognition pattern is more sensitive to the economic drivers of the contract.

(c) is conceptually consistent with market valuations of financial instruments and their pricing, both of which reflect the degree of risk associated with the financial instrument.

(d) will faithfully represent circumstances in which the entity has not charged sufficient premiums for bearing the risk that the claims might ultimately exceed expected premiums.

(e) will ensure that the measurement of an insurance contract includes a margin, which is essential to distinguish risk-generating liabilities from risk-free liabilities.

(f) will report changes in estimates about risk promptly and transparently.

BCA96 This Exposure Draft proposes that entities should consider the risk adjustment separately from the adjustment for the time value of money. The IASB observed that some existing accounting models combine these two adjustments by using risk-adjusted discount rates. However, that is not appropriate unless the risk is directly proportional to the amount of the liability and the remaining time to maturity. Insurance liabilities often do not have these characteristics. For example, the average risk in a portfolio of claims liabilities may rise over time

because more complex claims may take longer to resolve. Similarly, lapse risk may affect cash inflows more than it affects cash outflows. Moreover, risk adjustments generally reduce the value of future cash inflows but increase the value of future cash outflows. A single risk-adjusted discount rate is unlikely to capture these differences in risk.

A3. The following are relevant paragraphs from the Basis for Conclusions that explain the rationale behind the IASB's decision to recognise changes in the risk adjustment in profit or loss instead of recognising those changes by unlocking the contractual service margin.

Adjusting the contractual service margin for changes in the risk adjustment

BC36 The IASB proposes that all changes in the risk adjustment should be recognised immediately in profit or loss. In other words, the contractual service margin would not be adjusted for changes in the risk adjustment. However, changes in the risk adjustment contain three components: a release from risk as the coverage period expires, changes in risk that relate to future coverage periods and changes in risk that relate to incurred claims. Some argue that if the contractual service margin represents the unearned profit in the contract, it should be adjusted to reflect changes in the estimates of the risk associated with future coverage.

BC37 However, in the IASB's view:

(a) most changes in the risk adjustment would relate to the expiry of coverage. The change in risk adjustment relating to the expiry of coverage is the profit recognised from bearing risk in that period of coverage. Accordingly, such changes should be recognised in profit or loss.

(b) changes in risk relating to future coverage periods or changes in risk relating to incurred claims would arise when there are unexpected changes in circumstances. Changes in estimates of risks assumed in an insurance contract are critical to the measurement of the performance of commitments that are already underwritten. Recognising in profit or loss such changes in risk would provide more transparent information about those changes in circumstances.

(c) it would be difficult to disaggregate the overall change in risk in each period into:

  (i) the expiry of risk as coverage is provided; and

  (ii) the changes in estimates of risk associated with future coverage or incurred claims.

(d) changes in risk do not affect the amount of unearned profit relating to future coverage or services because they unwind over time.

Appendix B: Reasons for including an explicit risk adjustment in the measurement of the liability and cost-benefit assessment

B1. This Appendix provides further information on the background of why the IASB proposed an explicit risk adjustment as follows:

(a) why does the risk adjustment matter? (paragraphs B2–B6);

(b) when an explicit risk adjustment provides different information compared to an implicit risk adjustment (paragraphs B7–B9); and

(c) an assessment of costs and benefits of an explicit risk adjustment (paragraphs B10–B14).

Why does the risk adjustment matter?

B2. A simple example illustrates what a risk adjustment is intended to achieve. Consider two contracts:

(a) Contract A:

(i) claim payment – CU1,000,000 with a probability of 0.5; and

(ii) claim payment – CU0 with a probability of 0.5.

(b) Contract B:

(i) Claim payment – CU 500,000 with a probability of 1.

B3. As Table 1 shows, these two contracts have the same expected value:

Table 1

	Probability	Pay-off (CU)
A	0.5	1,000,000
	0.5	0
Probability-weighted average	**(0.5 × 1,000,000) + (0.5 × 1,000,000) = CU500,000**	
	Probability	**Pay-off (CU)**
B	1	500,000
Probability-weighted average	**(1 × 500,000) = CU500,000**	

B4. Thus, the expected value of cash flows in Contract A is the same as in Contract B. If an entity is indifferent to risk, it would value the cash outflows for Contract A and Contract B at the same amount. However, a risk-adverse entity would give more weight to the unfavourable scenarios than to the favourable ones. Therefore, all things being equal, a risk-adverse entity places a higher value on Contract B than on Contract A.

B5. A risk adjustment adjusts the expected value of cash flows to reflect the fact that a risk-adverse entity would assign different values to uncertain cash flows than to certain cash flows. Thus, the inclusion of a risk adjustment is consistent conceptually with the market valuations of financial instruments and their pricing, both of which reflect the degree of risk associated with the financial instrument.

B6. The IASB has previously concluded that an adjustment to reflect the difference in value that results from the effects of risk aversion would provide useful information about the risk inherent in the cash flows. Thus the ED proposes that the measurement of an insurance contract should include an explicit risk adjustment. Because the risk inherent in insurance contracts can vary over time, the risk adjustment proposed in the ED is remeasured at the end of each reporting period.

When does an explicit risk adjustment provide different information compared to an implicit risk adjustment?

B7. Table 2 compares an approach with an explicit risk adjustment to an approach with an implicit risk adjustment.

Table 2

	Explicit risk adjustment (ie risk adjustment plus contractual service margin)	**No explicit risk adjustment (ie a single margin)**	**Differences expected**
Type of measurement	• Explicit. • Fully re-measured to reflect the price and quantity of risk at each reporting date.	• Implicit – embedded in the calibration of the expected present value of cash flows to the initial pricing • Not subsequently remeasured, but allocated to profit or loss.	For a single margin approach, the change in uncertainty is reflected in the run-off of the margin and does not reflect changes in the price or quantity of risk.
Reporting of losses on day-one	• Considers an adjustment for risk in assessing whether there is a loss on day one.	• Does not consider an adjustment for risk in assessing whether there is a loss on day one.	When the risk adjustment is explicit, losses at inception are more likely to arise for some contracts.
How it reflects changes in risk	• Reflects increases in risk that exceed the allowance for risk included in the initial pricing of the contract.	• Measurement of risk capped at the initial composite margin, which is calibrated to the initial pricing of the contract.	The ratio of the risk adjustment to the contractual service margin may change after inception. Consequently, for some products, allocating a single margin in line with expected release from risk will result in a different pattern of amounts recognised in profit or loss compared to the changed in risk adjustment plus the allocation of the contractual service. In addition, for risky products with small margins, the margin may be exhausted more quickly (and subsequently rebuilt).

B8. In some cases, there are few differences on the effects of the financial statements between an approach with an explicit risk margin and one without. This would be the case:

(a) for the liability of remaining coverage, when

(i) the contract is not onerous, or is unlikely to be onerous, during the coverage period, and

(ii) the run-off pattern of the single margin is the same as the run-off pattern of the combined risk margin and contractual service margin.

Consequently, measuring the risk adjustment explicitly is less important when the amount of risk, even if significant, is expected to be recovered through the premiums charged and remains relatively constant or declines at a steady rate. For example, in a term-life contract in some jurisdictions, while the amount of risk may be significant, there are sufficient premiums charged for the risk and the risk does not typically fluctuate significantly during the coverage period, because mortality and lapse assumptions tend to be stable or change only very slowly.

(b) for the liability for incurred claims, when there is little variability in the amount of time that it takes to settle a claim and/or the final settlement payments. For example, this will be the case for most life contracts as they will typically be settled in less than a year.

B9. In other cases, there will be more significant differences in the amounts recognised in profit or loss and those recognised in the statement of financial position between approaches with and without an explicit risk adjustment, as follows:

(a) when contracts are onerous, because the entity has not charged a premium sufficient to cover the risks provided in the contract. Measuring an explicit risk margin will result in some contracts either being onerous at inception or will become onerous more quickly.

(b) when there are differences in the pattern of run-off of the contractual service margin and the change in risk adjustment. An implicit risk adjustment would not reflect the differences in run-off pattern because it would run off a combined risk adjustment and contractual service margin according to a single pattern. Under an explicit risk adjustment

approach, the risk adjustment is recognised in profit or loss according to the release of risk and the contractual service margin is run-off according to the provision of services

(c) when there is a significant period of time between the time that claims are incurred and the time that claims are settled, and there is significant variability in the expected cash flows that are needed to settle the claims.

Assessing costs and benefits

B10. Risk can vary, both between different types of contracts and for the same contract over time and/or over different jurisdictions. Accordingly, the IASB's previous conclusion was that more relevant information is provided to users of financial statements when risk is remeasured. Studies and previous rounds of fieldwork indicate that the risk adjustment will be larger and therefore more significant for:

(a) long-tail contracts (ie when claims take a long-time to settle). Long-tail contracts tend to occur more frequently for non-life contracts than life contracts, for example, contracts that cover asbestos, catastrophe, environmental liability or health (for example, long term care). The risk in such contracts can vary significantly over time as new information is obtained about the insured risk. For example:

(i) the amount of risk in a long-term health contract will significantly increase when policyholders become symptomatic for an unknown reason. As more information becomes available about the full effect and the extent of the illness, the amount of risk will decrease.

(ii) the development of new treatments may increase the risk of disability contracts if it is unclear whether the treatment can cure policyholders (so that they no longer claim) or merely prolong their lives (while leaving them in need of expensive ongoing treatment).

The risk adjustment is likely to be significant for the liability for incurred claims for non-life contracts. The majority of non-life contracts are likely

to be accounted for under the premium allocation approach with the minority accounted for under the general approach.

(b) cash flows that are affected by factors that are subject to greater variability. For example:

(i) lapse sensitive contracts, if there is a sudden trend that affects policyholder behavior. This will result in an increase in uncertainty if the full effect is unknown. For example, in some parts of the world, when the life expectancy started to increase, fewer policyholders surrendered long-term care insurance contracts than those that were initially estimated.

(ii) contracts that are dependent on changes in economic factors (for example, in periods of higher inflation, inflation-sensitive cash flows tend to be more uncertain as inflation is more volatile). A typical example is mortgage insurance contracts. During an economic crisis there will be more uncertainty about property values and policyholder behaviour (for example, policyholders defaulting to service their bonds due to job losses) than during a period of stability.

B11. In such cases the benefits of remeasuring an explicit risk adjustment are more apparent and the risk adjustment provides relevant information to users and can add to the understandability of the amount reported as insurance liabilities. In developing the ED, the IASB concluded that the benefits of this information would outweigh the costs of determining an explicit risk adjustment.

B12. The staff's recommendation to unlock the contractual service margin for changes in the risk adjustment relating to future coverage affects the assessment of costs and benefits. This is because information about changes in the risk adjustment would sometimes be shown in disclosures, rather than in profit or loss or as a change to the measurement of the insurance contract in the statement of financial position. This is a similar effect to adjusting the contractual service margin for changes in estimates of cash flows, for which the IASB has previously concluded that the information about changes in estimates presented in disclosures provides

useful financial information that outweighs the costs of re-estimation, even though there is no effect in profit or loss or the statement of financial position.

B13. Furthermore, the staff's recommendation to unlock the contractual service margin has a limited effect on the following situations in which an explicit risk adjustment provides useful financial information:

(a) for the liability for remaining coverage when contracts are, or become, onerous. For contracts that are onerous at inception, an explicit risk adjustment would provide the same information as would have been provided under the proposals in the ED. When contracts become onerous after inception, the risk adjustment would also provide information in profit or loss after the contract has become onerous.

(b) for the liability for incurred claims when there is no contractual service margin. For such cases, the same information would be provided under the staff recommendation as was provided under the proposals in the ED.

B14. The staff note that these are the situations in which an explicit risk adjustment would have provided the greatest benefit under the proposals in the ED. Because those benefits have not diminished, the staff conclude that the benefits of an explicit risk adjustment continue to exceed the costs of determining it.