



The Institute of Actuaries of Japan

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Sir David Tweedie
Chairman
International Accounting Standards Board
30 Cannon Street, London EC4M 6XH, United Kingdom

31 October, 2003

Dear Sir David:

On behalf of the Institute of Actuaries of Japan (IAJ), I am pleased to transmit the attached comments on the ED 5 Insurance Contracts prepared by IASB.

IAJ was founded in 1899, and present membership of IAJ numbers more than 3,600. IAJ is an organization to maintain, promote, and improve the ability of actuaries in Japan in performing the services of the actuarial profession and to contribute to the sound development of business related to the actuarial profession through holistic studies and research activities on actuarial science.

We would appreciate if you would think over our comments in developing International Accounting Standards.

Sincerely yours,

Motoyuki Terasaka

President

The Institute of Actuaries of Japan

IAJ Comments regarding ED5 "Insurance Contracts"

The Institute of Actuaries of Japan (IAJ) is pleased to submit comments on ED5 "Insurance Contracts" issued by the International Accounting Standards Board (IASB).

The Institute of Actuaries of Japan (IAJ) is an organization aiming to enhance professional skill of actuaries as well as to contribute to the sound development of the profession in the insurance business through wide-ranging research activities on actuarial science. We are not a trade association and we do not represent the interests of either clients or employers.

IAJ is a member of the International Actuarial Association (IAA), which is also planning to submit its comments on ED5. We, IAJ, submit our own comments for the following reasons:

- ED5 has important implications to the comprehensive standards which may have a serious impact on the insurance business; and
- ED5 essentially means continuous application of existing local GAAP. So it seems to have a lot of issues to be considered according to the situation in each jurisdiction.

We cordially hope that our comments here are of value for the IASB.

1. General Comments

IAJ, as a professional organization, has great interest in the Insurance Project and is willing to provide continuous assistance in developing the insurance IFRS through the IAA. In particular, we believe that further cooperation with actuaries and insurance regulators are essential for developing the comprehensive insurance accounting standards in phase . because the comprehensive standards may affect the structure of insurance business. Since involvement of actuaries and regulators is an important feature in the insurance industry, the IASB should further promote collaboration with the IAA and other related organizations.

We recognize that ED5 "Insurance Contracts" is expected to provide implications to the comprehensive standards and advance a step to develop the Insurance IFRS. We also recognize that it is expected to make limited improvements to what is not consistent with the Framework without requiring major changes that may need to be reversed, while continuing to apply existing local GAAP.

However, accounting practices for insurance are very diverse from one jurisdiction to another. It is, therefore, our concern that the ED5 may not reach its objectives to improve the insurance

accounting standards in the light of practice in each jurisdiction.

Our comments on the most important issues are as follows.

- (a) Accounting standards for insurance contracts are required to reflect properly the business reality as a whole. While we know that the IASB intends to show its commitment to complete phase. with the sunset clause, such standards that will automatically apply the Framework may make the direction of the accounting standards for insurance unclear, if the comprehensive standards in phase. will not have been completed in time. We recommend that the phase. should be maintained until the comprehensive standards are finalized.
- (b) Mismatch of asset and liability measurement is a very important issue to be solved in developing the comprehensive standards. In phase., when this issue has not been solved, some measures should be taken to reduce the misleading effect on the financial statements arising from the mismatch. Especially, ED5 should not prohibit taking such actions against mismatch in local GAAP.
- (c) It may cause confusions to prescribe requirements of disclosure concerning the “Fair Value of insurance liabilities” at present stage, where its contents and the measurement methods have not been clearly determined. In determining the “FV of insurance liabilities”, we note that there is no efficient secondary market of insurance and that various issues should be considered such as existing insurance practices in each jurisdiction and coordination with regulatory requirements.
- (d) Although we understand ED5’s intention to make the insurance accounting standards more useful with sufficient disclosure, we are afraid that its requirements are far more detailed than is required in other industries or actually required. Since significance of each disclosure varies in each jurisdiction in phase., where existing local GAAP are applied, the IASB should determine minimum requirements and leave the detailed or improved disclosure requirements to local GAAP so as to fit for each jurisdiction.

2. Comments on individual questions

The following are the comments on individual questions that the IAJ regards as especially important.

a. Question 1 – Scope

Mismatch of asset and liability measurement is a very important issue to be solved in developing the comprehensive standards. In phase., in which this issue has not been solved, some measures should be taken to reduce the misleading effect on the financial statements arising from the mismatch. Especially, ED5 should not prohibit taking such actions against mismatch in local GAAP.

b. Question 2 – Definition of insurance contract

Whether the definition is appropriate or not depends on the accounting model in the comprehensive standards. In view of the continuity of the accounting practice, the definition which may alter the scope of existing insurance contract in phase. is not desirable. One available solution to this issue is to define insurance contracts in phase. as “contracts treated as insurance in local GAAP”.

c. Question 3 – Embedded derivatives

We object to the unbundling requirements of the embedded derivatives, because the unbundling may not be required in phase. and it seems to make no sense to develop measurement system only for unbundling in phase.. Furthermore, even if material unrealized loss occurred in embedded derivatives, such loss could be captured in loss recognition tests.

d. Question 4 – Temporary exclusion from criteria in IAS 8

- (a) ED5 sets the limit for exemption as 31 December 2006. This inclusion of Sunset Clause may make the direction of insurance accounting unclear, if the comprehensive standards in phase. will not have been completed in time. We recommend that the phase. should be maintained until the comprehensive standards are finalized.
- (b) In some cases, catastrophe provisions include funds for possible future claims under current contracts. ED5 prohibit recognizing any catastrophe provisions as a liability but, in a strict sense, only the portions other than possible future claims under current contracts should be prohibited. If it is practically difficult to separate these portions, catastrophe provisions should not be eliminated.

e. Question 5 – Changes in accounting policies

The relevance and the reliability of changes in accounting policies should be judged by the accounting policy as a whole, not by individual tests prescribed in paragraph 14 – 17.

f. Question 6 – Unbundling

In phase., all the deposit components, not only those of traditional life insurance contracts, should be accounted according to each local GAAP. Although we understand the intention of ED5 to avoid the omission of assets and liabilities to be recognized, it is unclear if a criterion such as "to be recognized" is valid as intended in phase., where the measurement objectives are left to local GAAP.

g. Question 7 – Reinsurance purchased

In phase., accounting by a cedant for reinsurance should be based on existing local GAAP. Paragraph 18(d) and (e) of ED5 requires the measurement of each related portion of its liability under the direct insurance contract. However, in case of Excess of Loss Cover (ELC) reinsurance, for example, it is quite difficult to measure related liabilities under direct insurance contract layer by layer. Therefore, paragraph 18(d) and (e) of ED5 should be amended to apply only to specific reinsurance contracts in which comparison between the direct insurance and ceded reinsurance contract is obviously easy.

h. Question 8 – Insurance contracts acquired in a business combination or portfolio transfer

If measurement at acquisition is conducted under ED3, it may cause inconsistency with the subsequent measurements under existing local GAAP. So it should also be permitted to apply local GAAP for the contracts acquired in a business combination or portfolio transfer.

i. Question 9 – Discretionary participation feature

These features should be examined deeply in phase. of this project. It is not appropriate to determine the accounting for unallocated surplus in ED5 because we think it is a possible conclusion in phase. that establishing the intermediate category will fit for the comprehensive standards.

j. Question 10 – Disclosure of the fair value of insurance assets and liabilities

We object to the proposal for the FV disclosure of ED5 for the reason stated in the General Comments.

k. Question 11 – Other disclosures

Although we understand ED5's intention to make financial statements prepared under local standards more useful with sufficient disclosure, we are afraid that its requirements are far more detailed than is required in other industries and that the cost of meeting them exceeds the benefit derived from such disclosure. Consequently, it seems that ED5's objectives would not be achieved as intended. We also note that in phase., where local GAAP is

applied, in financial statements based on regulatory accounting such as in Japan, many of the disclosure requirements in ED5 represent different accounting objectives, not supplementary explanations. So, IASB should determine minimum requirements and leave the detailed or improved disclosure requirements to local GAAP so as to fit for each jurisdiction.