



## Memorandum

|                 |                              |                     |                |
|-----------------|------------------------------|---------------------|----------------|
| <b>To:</b>      | AASB members                 | <b>Date:</b>        | 20 August 2013 |
| <b>From:</b>    | Sue Lightfoot                | <b>Agenda Item:</b> | 14.1 (M133)    |
| <b>Subject:</b> | Insurance Contracts – Update | <b>File:</b>        |                |

### Action

For information – receive an update on the IASB’s Insurance Contracts project

Form preliminary views on the significant issues in IASB ED/2013/7 *Insurance Contracts* subject to considering any subsequent comment letters on AASB ED 244 (which incorporates IASB ED/2012/5) and comments from Roundtables.

Consider submissions on ED 241 *Amendments to AASB 1038 arising from AASB 10 in relation to consolidation and interests of policyholders* and provide staff with directions on amending AASB 1038.

### Attachments

Agenda paper 14.2 – Issues Paper on AASB ED 244 *Insurance Contracts*, incorporating IASB ED/2013/7 *Insurance Contracts*

Agenda paper 14.3 – Submissions on ED 244

Agenda paper 14.4 – Issues Paper on ED 241 *Amendments to AASB 1038 arising from AASB 10 in relation to consolidation and interests of policyholders* from Sue Lightfoot

Agenda paper 14.5 – Submissions on ED 241

### Overview

- 1 The AASB issued [ED 244](#) *Insurance Contracts* on 27 June 2013. ED 244 incorporates the IASB’s ED/2013/7 *Insurance Contracts*. Comments on ED 244 are due to the AASB by 27 September 2013 and comments are due to the IASB by 25 October 2013. ED 244 was provided to the AASB as Agenda Paper 9.2 at the July 2013 Board meeting. The [IASB Snapshot](#) on Insurance Contracts was also provided as Agenda Paper 9.3.
- 2 ED/2013/7 *Insurance Contracts* is a revision of ED/2010/8 *Insurance Contracts*, issued in June 2010 (which was incorporated into the AASB’s [ED 201](#)). The IASB has requested comments on the key areas it has changed as a result of feedback on ED/2010/8.

- 3 The following Roundtables have been scheduled to seek feedback from constituents on ED 244:

| Location               | Event  | Date                          |
|------------------------|--|-------------------------------|
| Sydney                 | Roundtable with participation of IASB Board members and IASB staff via videoconference | 3 September 2013<br>(4–6pm)   |
| Melbourne and Auckland | Joint Roundtable via videoconference   | 12 September 2013<br>(9–11am) |

- 4 AASB Board members are encouraged to attend either or both of the roundtables, particularly those who will be in Melbourne and/or Sydney at the relevant times.
- 5 Staff intend that the Board finalise its submission to the IASB on ED/2013/7 at the 23-24 October AASB meeting, with the benefit of feedback received from any comment letters received on ED 244 and comments received at the roundtables.

## Background

- 6 The model proposed in ED/2013/7 includes some significant differences from the model proposed in the IASB’s ED/2010/8 *Insurance Contracts* and these are the main areas the IASB is seeking comment on. They include the following proposed requirements:
- (a) remeasurement of service margins included in insurance liabilities;
  - (b) a measurement and presentation exception for contracts with a specified link between policyholder returns and returns on underlying items (‘mirroring’)
  - (c) presentation of insurance contract revenues and expenses (rather than net movements in those flows) in the income statement;
  - (d) presentation of the impact of changes in discount rates on insurance liabilities in other comprehensive income; and
  - (e) retrospective application on transition when it is practicable.

There are further proposals on which the IASB is not explicitly seeking comment that could have significant implications for Australian practice, including the proposals on ‘contract boundary’ and acquisition costs.

- 7 In preparation for the adoption of IFRS by a number of jurisdictions, including Australia, in 2005, the IASB introduced an interim standard (IFRS 4 *Insurance Contracts* – adopted as AASB 4 *Insurance Contracts* in Australia) until a more comprehensive review of the accounting for insurance contracts could be completed. Because IFRS 4/AASB 4 is an interim standard, it grandfathers much of the accounting practiced prior to adopting IFRS and therefore AASB 1023 *General Insurance Contracts* and AASB 1038 *Life Insurance Contracts* (modified to be consistent with AASB 4) remain in force.

- 8 The proposed IFRS that emerges from ED/2013/7, if adopted in Australia, would be expected to replace the existing AASB 4, AASB 1023 and AASB 1038.
- 9 Some of the key differences between the proposals in the IASB's ED/2013/7 and the existing Australian Accounting Standards, AASB 4, AASB 1023 and AASB 1038, are outlined below.

*(a) Insurance contract boundary*

ED/2013/7 proposes an underlying notion of the boundary of an insurance contract, which may have an impact on current Australian practice, in particular, in regard to some types of term life insurance contracts. The proposal is that the boundary of an insurance contract be determined by reference to the extent to which the insurer can compel the policyholder to pay the premiums or has a substantive obligation to provide the policyholder with coverage or other services. In general terms, a substantive obligation to provide coverage or other services would end when the insurer has the right or the practical ability to reprice the risks involved in a contract or portfolio of contracts.

*(b) Acquisition costs*

ED/2013/7 proposes that insurers include incremental acquisition costs in the present value of future cash flows under the contract and that all acquisition costs other than incremental acquisition costs be recognised as an expense when incurred. This contrasts with the requirements in AASB 1023 to defer and recognise as assets those costs that can be reliably measured and for which it is probable they will give rise to premium revenue that will be recognised in the income statement in subsequent reporting periods. Under AASB 1023, those deferred costs are subsequently amortised.

*(c) Impact of a change of discount rates*

ED/2013/7 proposes that (with the exception of 'investment linked' business) insurers recognise and present in other comprehensive income (OCI) the difference between: (a) an insurance contract liability discounted for the time value of money (as described in the ED) at the date the contract(s) were initially recognised; and (b) the insurance contract liability discounted for the time value of money at the reporting date. Accordingly, the impact of any change in the discount rate is presented in OCI, whilst the rest of any change in insurance contract liabilities is presented in profit or loss. Under AASB 1023 and AASB 1038 these changes are all recognised and presented in profit or loss.

*(d) Revenue recognition*

ED/2013/7 proposes that insurers recognise premium revenue and expenses as they relate to each period. This is consistent with the 'premium deferral' model in AASB 1023, but would be a significant change from AASB 1038 under which premium revenue is recognised when the premiums are controlled (generally when received).