Australian Government
Australian Accounting Standards Board

Memorandum

To:	**AASB members**	**Date:**	1 July 2014
From:	**Sue Lightfoot**	**Agenda Item:**	13.1 (M139)
Subject:	**Insurance Contracts: Project Update**	**File:**	

Action

Consider key issues arising from recent IASB meetings on its Insurance Contracts project, and decide whether there are any issues that need to be raised with the IASB at this stage.

Background

In November 2010, the AASB issued ED 201 *Insurance Contracts*, which incorporated the IASB's exposure draft, ED/2010/8 *Insurance Contracts*. The comment period for IASB's ED/2010/8 closed on 30 November 2010 (the comment period for AASB ED 201 closed on 8 November 2010 and attracted 17 submissions).

The AASB submission to the IASB on ED/2010/8, dated 2 December 2010, can be located on the AASB website here.

At AASB meetings held since 2010, AASB staff provided regular updates on the project incorporating tentative decisions made by the IASB.

The IASB subsequently decided to re-expose revised proposals. In June 2013, the AASB issued ED 244 *Insurance Contracts*, which incorporated the IASB's revised exposure draft, ED/2013/7 *Insurance Contracts*. The comment period for IASB's ED/2013/7 closed on 25 October 2013 and 194 comment letters were received (the comment period for AASB ED 244 closed on 27 September 2013 and attracted 12 submissions).

The revised ED sought input on five areas for which the IASB made significant changes in response to the feedback it received on its proposals in the 2010 Exposure Draft, as follows:

a) Adjusting the contractual service margin;

b) Contracts that require the entity to hold underlying items and specify a link to returns on those underlying items;

c) Presentation of insurance contract revenue and expense;

d) Interest expense in profit or loss; and

e) Effective date and transition.

The AASB submission to the IASB, dated 31 October 2013, can be located on the AASB website here.

IASB Redeliberations on ED/2013/7

The IASB began redeliberations on ED/2013/7 in January 2014 and began making tentative decisions at its March 2014 meeting. An analysis of the IASB's tentative decisions to date on ED/2013/7 is included in the Appendix to this memorandum. Page references to the Appendix are shown below. Note that the comments in the Appendix regarding the March and April meetings are provided again for information only.

Prior to its June meeting the IASB considered only contracts that have no participating features. The IASB has indicated that those tentative decisions may be revisited at a later stage as a result of its consideration of participating contracts. As at the date of this memorandum, no tentative decisions have been made concerning participating contracts.

March 2014 (pages 5-8)

In its March 2014 the IASB discussed:

- unlocking the contractual service margin; and
- recognising the effects of changes in the discount rate in other comprehensive income.

The Board had written a letter to the IASB in late April expressing concern about the IASB's tentative decision to require, for all portfolios of insurance contracts, disclosure of the difference between the present value of changes in expected cash flows that adjust the contractual service margin (CSM) in a reporting period:

a) when measured using discount rates that applied on initial recognition of insurance contracts; and

b) when measured at current rates.

The response (agenda paper 3.6 of the May AASB meeting) from the IASB Chairman indicated that the IASB intends to reconsider the use of discount rates that applied on initial recognition of insurance contracts, which may lead to a change in the disclosure requirements. As at the date of this memorandum, that reconsideration has not yet taken place.

April and May 2014 (pages 9-15 and pages 16-17)

In its April 2014 meeting, the IASB considered:

- presentation of insurance contract revenue; and
- the proposed approach to other issues raised in the response to the 2013 ED that were unrelated to the five specific areas focussed on by ED/2013/7.

In its May 2014 meeting, the IASB considered:

- recognising the contractual service margin in profit or loss; and
- fixed-fee service contracts, significant insurance risk, portfolio transfers and business combinations.

At its May 2014 meeting, the AASB decided to raise concerns with the IASB in relation to three tentative decisions made at the IASB's April and May 2014 meetings regarding non-participating contracts. Those tentative decisions were:

1. not to re-consider disclosures in future meetings;

2. not to consider the unbundling-lapse together 'rule' in future meetings; and

3. to clarify that the service represented by the CSM is insurance coverage that is provided on the basis of the passage of time and reflects the number of contracts in force.

In relation to the third concern above, the Board expressed the view that the IASB's decision to use coverage period for allocating CSM (for non-participating businesses) has three flaws or weaknesses:

a) the allocation would not reflect a pattern of meeting a stand-ready obligation (for example, for Lenders Mortgage Insurance where the service is typically non-linear);

b) the allocation would be inconsistent with the outcome under the simplified premium allocation approach; and

c) insurers do not currently perform this calculation.

The Board considered that using value of expected claims would address all of the above flaws or weaknesses.

The above concerns were raised with the IASB and IASB staff at the Accounting Standards Advisory Forum on 2 June 2014 and a follow up letter will be sent to the IASB reiterating the concerns by the date of the AASB meeting.

The AASB determined that there were no other issues it wished to raise with the IASB at that stage.

<u>June 2014 (pages 18-20)</u>

The IASB met on 17 June 2014 and, in particular, discussed the following:

- contracts with participating contracts[1];

- discount rates when there is no observable market;

- asymmetric treatment of reinsurance gains; and

- level of aggregation.

1 The IASB continued its discussions on contracts with participating features by considering how it might limit the application of any alternative adaptations that it might make to its general model for insurance contract, when those adaptations would rely on the identification of the underlying items. IASB staff were directed to consider whether an entity should adjust the CSM for changes in the insurer's share of the underlying items on the grounds that the insurer's share represents an implicit management fee, and whether an entity should apply a 'book yield' approach for determining the interest expense presented in profit or loss. The mechanics of the book yield approach were also to be further explored by staff.

Next steps

The IASB will continue its redeliberations at its July meeting. Staff expect that redeliberations of the proposals will be completed in 2014, with the publication of a final Standard following in 2015.

Staff recommendation

Staff consider that, aside from the issues previously identified, there are no further issues to be raised with the IASB at this stage.

Staff will continue to monitor the project.

Question to Board members:
Does the Board agree with the staff recommendation?

IASB Tentative Decisions on Insurance Contracts (concerning non-participating contracts only)

IASB Tentative Decisions	**Comment from AASB Submission to IASB (emphasis added in bold)**	**AASB staff comment**
March 2014		
Unlocking the contractual service margin (CSM)		
(a) to confirm the proposals in ED/2013/7 that after inception: (i) differences between the current and previous estimates of the present value of cash flows related to future coverage and other future services should be added to, or deducted from, the contractual service margin, subject to the condition that the contractual service margin should not be negative; and (ii) differences between the current and previous estimates of the present value of cash flows that do not relate to future coverage and other future services should be recognised immediately in profit or loss.	1.1 The AASB supports the proposal that **the impact on the CSM of a difference between assumed and actual experience is recognised immediately in profit or loss on the basis that it relates to risks borne in the period. The AASB also supports the proposal that the impact on the CSM of a change in assumptions is recognised as an adjustment to the CSM on the basis that it relates to risks to be borne in future periods** and can be regarded as akin to a new policy being written at reporting date for the remaining period of the relevant contracts. 1.2 The AASB **supports the proposal that the CSM cannot be negative** (paragraph 30(d)(ii)) **and that any further projected deterioration is recognised immediately in profit or loss** (paragraph 31)...	The IASB tentative decisions are in line with the comments from the AASB.
(b) that favourable changes in estimates that arise after losses were previously recognised in profit or loss should be recognised in profit or loss to the extent that they reverse losses that relate to coverage and other services in the future.	1.2 …However**, the AASB recommends that the IASB also address accounting the reversal of circumstances that gave rise to losses. The AASB would expect this to involve reversing the effects of previous loss recognition,** which (depending on the extent of subsequent improvements in expected cash flows related to future coverage) **could involve recognising gains in profit or loss and** 'rebuilding' the CSM. This would be consistent with the	The IASB tentative decisions are in line with the comments from the AASB.

IASB Tentative Decisions	Comment from AASB Submission to IASB (emphasis added in bold)	AASB staff comment
	requirements for the reversal of impairment losses in IAS 36 Impairment of Assets and the requirements for the reversal of provisions in IAS 37 *Provisions, Contingent Liabilities and Contingent Assets.*	
(c) that differences between the current and previous estimates of the risk adjustment that relate to future coverage and other services should be added to, or deducted from, the contractual service margin, subject to the condition that the contractual service margin should not be negative. Consequently, changes in the risk adjustment that relate to the coverage and other services provided in the current and past periods should be recognised immediately in profit or loss.	1.12 The AASB notes that a likely major source of future profits relates to bearing risk in future periods. Accordingly, the AASB recommends that an improvement be made to the proposals to require **a change in the risk margin relating to future coverage to be adjusted to the CSM**. **The change in the risk margin that relates to past coverage would continue to be required to be recognised in profit or loss immediately**. For those entities that consider it is not feasible to allocate changes in the risk margin between that which relates to past and future coverage, the AASB recommends that the IASB provides an 'impracticability' concession similar to that proposed as part of the transition requirements.	The IASB tentative decisions are in line with the comments from the AASB.
Recognising the effects of changes in the discount rate in other comprehensive income (OCI)		
(a) that an entity should choose to present the effect of changes in discount rates in profit and loss or in other comprehensive income as its accounting policy and should apply that accounting policy to all contracts within a portfolio, subject to developing: (i) guidance that entities should apply the same accounting policy to groups of similar portfolios, and (ii) guidance that this would provide rigour about when entities could change accounting policies based on the requirements for changing	4.1 …**the AASB recommends that the IASB 'default' requirement should be a current measurement basis for insurance liabilities with changes recognised in profit or loss (or CSM as applicable). However the AASB could support the IASB providing an option to present changes in discount rate in OCI that insurers could elect to use** for insurance activities of an entity on transition to the revised insurance contracts standard.	The IASB tentatively decided that there would be no default approach (between profit or loss or OCI) to presentation of changes in the effect of the discount rate of insurance contract liabilities. The effect of the tentative decision is similar to the recommendation of the AASB in supporting both profit or loss and

IASB Tentative Decisions	Comment from AASB Submission to IASB (emphasis added in bold)	AASB staff comment
accounting policy in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. (b) If the entity chooses to present the effect of changes in discount rates in other comprehensive income, that an entity should recognise: (i) in profit or loss, the interest expense determined using the discount rates that applied at the date that the contract was initially recognised; and (ii) in other comprehensive income, the difference between the carrying amount of the insurance contract measured using the discount rates that applied at the reporting date and the carrying amount of the insurance contract measured using the discount rates that applied at the date the contract was initially recognised.		OCI presentation to be available. However the AASB had a number of concerns about the use of OCI – see below.
(c) that an entity should disclose the following information: (i) *For all portfolios of insurance contracts*: an analysis of total interest expense included in total comprehensive income disaggregated at a minimum into: 1 the amount of interest accretion determined using current discount rates; 2 the effect on the measurement of the insurance contract of changes in discount rates in the period; and 3 the difference between the present value of	The comment in paragraphs 4.16 to 4.18 below were given in the context of presenting amounts in OCI, however also appears applicable to the IASB's tentative decisions on disclosure: *Tracking* 4.16 **The proposal would involve identifying and tracking discount rates from contract inception for the life of a policy or claims liability,** which could be up to 60 years. 4.17 In theory, the unit of account should be either each contract or a portfolio of similar contracts determined by when the discount rate changes in a manner that would have a material impact, which could be many times within a reporting period. Otherwise, the	AASB staff are concerned that the disclosure in c) i) 3 are inconsistent with an approach of recognising changes in insurance contract liabilities in profit or loss. A second reason for the concern is that in order to determine the amounts to disclose, an entity would need to identify and track discount rates from contract inception for the life of a policy or claims liability. Therefore despite not being required to determine an amount

IASB Tentative Decisions	Comment from AASB Submission to IASB (emphasis added in bold)	AASB staff comment
changes in expected cash flows that adjust the contractual service margin in a reporting period when measured using discount rates that applied on initial recognition of insurance contracts, and the present value of changes in expected cash flows that adjust the contractual service margin when measured at current rates. (ii) In addition, for portfolios of insurance contracts for which the effect of changes in discount rates are presented in other comprehensive income: an analysis of total interest expense included in total comprehensive income disaggregated at a minimum into: 1 interest accretion at the discount rate that applied at initial recognition of insurance contracts reported in profit or loss for the period; and 2 the movement in other comprehensive income for the period.	objective of an amortised cost interest expense would not be met. 4.18 However, presumably, entities would need to take a pragmatic view the unit of account employed for tracking discount rates to make systems costs manageable. That pragmatic view might involve quarterly or half-yearly cohorts. Even so insurers are likely to have hundreds, and possibly tens of thousands, of cohorts of contracts to track. And different entities are likely to come to different pragmatic solutions creating another source of non-comparability. **Depending on how the IASB explains the unit of account for tracking discount rates, the systems issues for insurers could be overwhelming.** 9.1 The AASB is also concerned about the proposed disclosures, which we consider are too detailed and would clutter the financial statements. **The AASB supports disclosure of the key amounts underlying the changes in insurance liabilities for the period, including that due to changes in discount rate and other significant drivers of the result if material**. In particular, the requirements for reconciliations in paragraphs 74 to79 of ED/2013/7 seem particularly burdensome. 9.2 …the AASB encourages the IASB to rationalise the extent of identified disclosures.	to be recognised in OCI, an entity would still be required to put in place systems and processes to calculate that amount. The AASB comment letter supported disclosure of key amounts for the period – rather than amounts tracked from contract inception.

IASB Tentative Decisions	Comment from AASB Submission to IASB (emphasis added in bold)	AASB staff comment
April 2014		
Insurance Contract Revenue		
to confirm the 2013 ED proposals that an entity: a) should present insurance contract revenue and expense in the statement of comprehensive income, as proposed in paragraphs 56–59 and B88–B91 of the 2013 ED; and	3.1 Current Australian GAAP[2] bears some similarities to the ED/2013/7 proposals (at a high level with BBA being analogous to AASB 1038 *Life Insurance Contracts*[3] and PAA being analogous to AASB 1023 *General Insurance Contracts*)[4]. However, Australian life insurers would be particularly affected by the proposals as they would need to change their systems to recognise only revenue related to risks borne in the period. 3.2 The AASB supports the proposals as the presentation proposed would generally bring all insurers in line with non-insurers. As noted in paragraph BC76, of ED/2013/7 the proposals should be broadly consistent with the general principles in the IASB's 2011 Exposure Draft *Revenue from Contracts with Customers*, such that an entity would recognise the consideration to which the entity expects to be entitled in exchange for the coverage and other services, as it satisfies its performance obligations. Furthermore, aligning presentation with non-insurers allows	The IASB tentative decisions are in line with the comments from the AASB.

2 Under AASB 1038 premiums received are recognised as revenue and a claims liability (and related expense) is also recognised based on a prospective cash flows approach (similar to BBA under ED/2013/7). Under AASB 1023 premium revenue is recognised over the period of the contract based on the pattern of the incidence of risk expected. The initial claims liability is the deferred premium (similar to PAA under ED/2013/7). Paragraph 9.1 of AASB 1023 imposes a liability adequacy test and, if the present value of expected cash flows exceeds unearned premium, a loss is recognised immediately.

3 AASB 1038 paragraphs 16.1, 17.1, 17.2 and 18.1, require a substantial number of disclosures relating to the statement of income and they are too numerous to list here. Suffice to say, the income statement includes revenues recognised and the focus of most of the note disclosures is on the components of the changes in claims liabilities.

4 AASB 1023 paragraph 17.1, requires the following, and implies that they should be presented on the face of the income statement: premium revenue (direct); reinsurance premium revenue; reinsurance and other recoveries; net claims incurred showing separately: a) the amount for risks borne in current period; and b) the amount for reassessment of risks borne in previous periods; underwriting result; gross claims incurred (undiscounted); and reinsurance and other recoveries (undiscounted).

IASB Tentative Decisions	Comment from AASB Submission to IASB (emphasis added in bold)	AASB staff comment
	diversified financial institutions to present information on a similar basis, rather than presenting insurance related items in a different manner. 3.3 Feedback from Australian constituents indicates that there is broad support for these proposals and this approach is preferred to the 'summarised margin' approach of ED/2010/8.	
to confirm the 2013 ED proposals that an entity: b) should disclose the following: (i) a reconciliation that separately reconciles the opening and closing balances of the components of the insurance contract asset or liability (paragraph 76 of the 2013 ED); (ii) a reconciliation from the premiums received in the period to the insurance contract revenue in the period (paragraph 79 of the 2013 ED); (iii) the inputs used when determining the insurance contract revenue that is recognised in the period (paragraph 81(a) of the 2013 ED); and (iv) the effect of the insurance contracts that are initially recognised in the period on the amounts that are recognised in the statement of financial position (paragraph 81(b) of the 2013 ED).	9.1 The AASB is also concerned about the proposed disclosures, which we consider are too detailed and would clutter the financial statements. The AASB supports disclosure of the key amounts underlying the changes in insurance liabilities for the period, including that due to changes in discount rate and other significant drivers of the result if material**. In particular, the requirements for reconciliations in paragraphs 74 to79 of ED/2013/7 seem particularly burdensome**. 9.2 …the AASB encourages the IASB to rationalise the extent of identified disclosures to alleviate this burden. **For example, in paragraph 74, there seems little justification for requiring separate reconciliations for insurance contracts in a liability position and insurance contracts in an asset position.** One portfolio might give rise to a small asset and could change from an asset to a liability position from period to period. Also, given the number of portfolios that would be aggregated into a reconciliation in a large insurer, the presentation of two reconciliations would have little or no information value.	The IASB tentative decisions appear to result in reduced mandated disclosure than was proposed in ED/2013/7. This reduction in disclosure is in line with the comments from the AASB. [For example, the following disclosures were included in the ED but the IASB <u>has not</u> specified that they would be retained: Pgh 74 – reconciliations showing how the carrying amounts of insurance contracts that are in a liability position and insurance contracts that are in an asset position are affected by cash flows and income and expenses recognised in profit or loss and other comprehensive income. Pgh 75 – reconciliations showing how the aggregate carrying amounts of reinsurance contracts held in an asset position and

IASB Tentative Decisions	Comment from AASB Submission to IASB (emphasis added in bold)	AASB staff comment
		reinsurance contracts held in a liability position are affected by cash flows and income and expense presented in profit or loss. Pgh 81(a) - For contracts to which the premium allocation approach is not applied the entity shall disclose: (a) the following inputs that are used when determining the insurance contract revenue that is recognised in the period: (i) the expected cash outflows for the period, excluding investment components; (ii) the acquisition costs that are allocated to the period; (iii) the change in risk adjustment in the period; and (iv) the amount of the contractual service margin recognised in the period.]
an entity should be prohibited from presenting premium information in the statement of comprehensive income if that information is not consistent with commonly understood notions of revenue.		AASB staff consider that it is not clear what this tentative decision means in practice as commonly understood notions of revenue' is not defined and there may be a variety of commonly understood

IASB Tentative Decisions	Comment from AASB Submission to IASB (emphasis added in bold)	AASB staff comment
		notions of revenue in existing GAAP. However, the AASB staff support the principle that revenue from insurance contracts should be recognised in a manner consistent with the forthcoming Standard IFRS 15 *Revenue from Contracts with Customers*.
Project plan for the non-targeted issues		
a) to consider in future meetings the following non-targeted issues: (i) references to 'unit of account' and 'portfolio' in the 2013 ED and whether it will be possible to clarify the IASB's intentions and provide more consistency; (ii) whether to provide further guidance regarding discount rate for long-term contracts when there is little or no observable market data; (iii) whether in some circumstances there is an accounting, rather than an economic mismatch between insurance contracts and reinsurance contracts because of the asymmetrical treatment of their contractual service margins, and if so, whether such a mismatch could be mitigated; (iv) whether to provide more guidance on an appropriate allocation pattern for the contractual service margin; (v) whether to provide guidance for the significant insurance risk definition for a specific contract; (vi) whether the requirements for portfolio transfers		AASB staff agree that the IASB should consider these topics in future meetings.

IASB Tentative Decisions	Comment from AASB Submission to IASB (emphasis added in bold)	AASB staff comment
and business combinations could be simplified and clarified; and (vii) whether to provide an option for fixed-fee service contracts.		
b) not to consider in future meetings other non-targeted issues, including those relating to: (i) disclosures; (ii) premium allocation approach; (iii) combination of insurance contracts; (iv) contract boundary for specific contracts; (v) unbundling—lapse together criteria; (vi) treatment of ceding commissions; (vii) discount rate—top-down and bottom-up approaches; (viii) tax included in the measurement; and (ix) combining the contractual service margin with other comprehensive income.	**ED/2013/7 Other issues: Disclosure** Refer paragraph 9.1 to 9.2 above. **ED/2013/7 Other issues: Separating insurance contracts from investment contracts ('unbundling')** 8.1 Insurance and investment services are often bundled together with investment contracts. ED/2013/7 paragraph 10(b) requires an entity to separate a distinct investment component from a host insurance contract on the basis set out in Appendix B. 8.2 Paragraph B31 sets out a principle that 'unless the investment component and insurance component are highly interrelated, an investment contract is distinct if a contract with equivalent terms is sold, or could be sold, separately in the same market or jurisdiction by the entity or any other entity'. Paragraph B32 goes on to provide indications of when an investment component and insurance component would be considered highly interrelated. 8.3 The AASB supports this proposed principle. However, **sub-paragraph 32(b) introduces a proposed rule that overrides the principle – that if the lapse or maturity of one component in a contract causes the lapse or maturity of the other, the entity must treat the whole contract as an insurance contract. The AASB considers that this condition should only be an indicator that helps**	<u>(i) Disclosures</u> In paragraphs 9.1 to 9.2 of the AASB's submission to the IASB on ED/2013/7, the AASB expressed concerns with the proposed disclosures. AASB staff also note that the letter from Hans Hoogervorst dated 29 April 2014 indicated that disclosure decisions may be revised in due course. AASB staff think that the IASB should consider disclosures at the end of its redeliberations, in light of the collective decisions made to that point. <u>(v) Unbundling</u> As set out in paragraphs 8.1 to 8.5 of the AASB's submission to the IASB on ED/2013/7, AASB staff consider that the IASB should also reconsider the lapse together criteria for unbundling.

IASB Tentative Decisions	Comment from AASB Submission to IASB (emphasis added in bold)	AASB staff comment
	elucidate the principle. 8.4 The proposed rule would mean that some contracts in Australia that are currently unbundled into their insurance and investment components would not be able to be unbundled. An example is a product that involves an investment account that is charged with the relevant insurance premiums, and when a client terminates the investment contract element there is no longer an account from which premiums are charged. Accordingly, the whole contract lapses and clients wishing to continue the insurance component are sold a 'new' policy. However, for the duration of the bundled policy, there are two distinct components that are quite capable of being separately recognised based on their natures. 8.5 ED/2013/7 paragraph B25 includes a further proposed rule that compounds the problem caused by the rule in sub-paragraph B32(b). The further rule states: a contract that meets the definition of an insurance contract remains an insurance contract until all rights and obligations are extinguished. That would mean a contract that is regarded as an insurance contract at inception must always be treated as an insurance contract, even though there are products that at inception are substantially insurance contracts which, over time, become substantially investment contracts. 8.6 The proposals have the potential to seriously distort the financial statements of insurers by requiring investment components of contracts to be treated as insurance contracts. This would be a particular problem for entities that have multiple activities such as banking, wealth management and insurance. The same product sold by the entity as a stand-alone	

IASB Tentative Decisions	Comment from AASB Submission to IASB (emphasis added in bold)	AASB staff comment
	wealth management product to one customer and as part of a contract that includes an insurance component to another customer could be treated differently. 8.7 The distortion might be revealed in a reconciliation to segment disclosures (required by paragraph 28 of AASB 8 Operating Segments) because Australian entities that sell bundled products generally unbundle them into their insurance segments and wealth segments for management information purposes. However, the AASB considers that it is inappropriate to have potentially misleading accounting in the primary financial statements and then have to effectively correct the picture provided through segment disclosure.	

IASB Tentative Decisions	Comment from AASB Submission to IASB (emphasis added in bold)	AASB staff comment
May 2014		
Recognising the contractual service margin in profit or loss		
a) confirm the principle in the 2013 ED that an entity should recognise the remaining contractual service margin in profit or loss over the coverage period in the systematic way that best reflects the remaining transfer of the services that are provided under an insurance contract. b) clarify that, for contracts with no participating features, the service represented by the contractual service margin is insurance coverage that: (i) is provided on the basis of the passage of time; and (ii) reflects the expected number of contracts in force.	No specific comments in the AASB submission other than the comment below: 1.1 The AASB supports the proposal that the impact on the CSM of a difference between assumed and actual experience is recognised immediately in profit or loss on the basis that it relates to risks borne in the period. **The AASB also supports the proposal that the impact on the CSM of a change in assumptions is recognised as an adjustment to the CSM on the basis that it relates to risks to be borne in future periods and can be regarded as akin to a new policy being written at reporting date for the remaining period of the relevant contracts.**	As noted in the Action Alert for the May 2014 AASB meeting, the Board decided to raise its concerns in relation to the IASB's tentative decision to clarify that the service represented by the CSM is insurance coverage that is provided on the basis of the passage of time and reflects the number of contracts in force. The AASB expressed the view that the IASB's decision to use coverage period for allocating CSM (for non-participating businesses) has three flaws or weaknesses: (a) the allocation the allocation would not reflect a pattern of meeting a stand-ready obligation (for example, for Lenders Mortgage Insurance where the service is typically non-linear); (b) the allocation would be inconsistent with the outcome under the simplified premium allocation approach; and

IASB Tentative Decisions	Comment from AASB Submission to IASB (emphasis added in bold)	AASB staff comment
May 2014		
Recognising the contractual service margin in profit or loss		
		(c) insurers do not currently perform this calculation. The Board considered that using value of expected claims would address all of the above flaws or weaknesses and this approach should be raised with the IASB.
Fixed-fee service contracts, significant insurance risk, portfolio transfers and business combinations		
a) that entities should be permitted, but not required, to apply the revenue recognition Standard to the fixed-fee service contracts that meet the criteria in paragraph 7(e) of the 2013 ED. b) to clarify the guidance in paragraph B19 of the 2013 ED that significant insurance risk only occurs when there is a possibility that an issuer will incur a loss on a present value basis. c) to clarify the requirements for contracts acquired through a portfolio transfer or a business combination in paragraphs 43-45 of the 2013 ED, that such contracts should be accounted for as if they had been issued by the entity at the date of the portfolio transfer or business combination.	No specific comment in the AASB submission.	No issues noted with the tentative decisions on this topics.

IASB Tentative Decisions	Comment from AASB Submission to IASB (emphasis added in bold)	AASB staff comment
June 2014		
Discount rates for long-term contracts when there are few or no observable market data		
a) confirm the principle that the discount rates used to adjust the cash flows in an insurance contract for the time value of money should be consistent with observable current market prices for instruments with cash flows whose characteristics are consistent with those of the insurance contract; and b) provide additional application guidance that, in determining those discount rates, an entity should use judgement to: (i) ensure that appropriate adjustments are made to observable inputs to accommodate any differences between observed transactions and the insurance contracts being measured. (ii) develop any unobservable inputs using the best information available in the circumstances, while remaining consistent with the objective of reflecting how market participants assess those inputs. Accordingly any unobservable inputs should not contradict any available and relevant market data.	1.3 The AASB supports the IASB's proposals to discount estimates of fulfilment cash flows and also supports the IASB allowing a 'bottom-up' or 'top-down' approach to be used for determining the discount rates to use. Although this may lead to reduced comparability this would enable entities to select a method of determining discount rates which is most reliable and practical for them. 1.4 On the face of it, the requirement to discount cash flows does not seem dissimilar to current Australian requirements. However, the discount rates proposed in the ED are likely to be somewhat different from those currently being employed by Australian insurers. Australian insurers would therefore be likely to require some changes to existing systems in order for them to adopt the proposals. The key difference between the proposals compared to current Australian GAAP on insurance contracts is the explicit consideration of liquidity risk (although the AASB notes that currently some life insurers already incorporate liquidity risk in their discount rate). The AASB supports the IASB's proposal to require liquidity risk to be considered, to enhance comparability between entities.	Staff consider that the tentative decisions made are reasonable and would provide useful guidance on how to consider observable and unobservable inputs when determining the appropriate discount rate to use.

IASB Tentative Decisions	Comment from AASB Submission to IASB (emphasis added in bold)	AASB staff comment
Asymmetrical treatment of gains from reinsurance		
After inception, an entity should recognise in profit or loss any changes in estimates of fulfilment cash flows for a reinsurance contract that an entity holds when those changes arise as a result of changes in estimates of fulfilment cash flows for an underlying direct insurance contract that are recognised immediately in profit or loss.	No specific comment in the AASB submission.	Staff agree that the recognition of changes of fulfilment cash flows of reinsurance contracts should be recognised in profit or loss when the change in the underlying contracts are recognised in profit or loss to allow the amounts to be recognised in profit or loss at the same time.
Level of aggregation		
a) clarify that the objective of the proposed insurance contracts Standard is to provide principles for the measurement of an individual insurance contract, but that in applying the Standard an entity could aggregate insurance contracts provided that it meets that objective. b) amend the definition of a portfolio of insurance contracts to be: "insurance contracts that provide coverage for similar risks and are managed together as a single pool"; and c) add guidance to explain that in determining the contractual service margin or loss at initial recognition, an entity should not aggregate onerous contracts with profit-making contracts. An entity should consider the facts and circumstances to determine whether a contract is onerous at initial recognition. To provide examples on how an entity could aggregate contracts but nonetheless satisfy the objective in a. above when determining the contractual service margin at a	No specific comment in the AASB submission on ED/2013/7, however the following comment was made in the AASB submission on ED/2010/8: 31 The proposal to aggregate residual margins on the basis of portfolios of contracts that have similar dates of inception and similar coverage periods helps to enforce the notion that residual margins are locked in (potentially year-by-year), thereby facilitating application of proposal to systematically run residual margins off to profit or loss. However, we note that these proposals have a number of other consequences. **In particular, restricting portfolios to groups of contracts that:** **a) are subject to broadly similar risks and managed together by the insurer as a single pool; and** **b) have similar dates of inception (short-duration insurance contracts); or** **c) have similar dates of inception and similar coverage periods (all insurance contracts**	Staff consider that the tentative decision to allow aggregation by portfolio, where the portfolio is based on similar risks and management as a single pool is reasonable, and is consistent with comments made by the AASB in its submission on ED/2010/8.

IASB Tentative Decisions	Comment from AASB Submission to IASB (emphasis added in bold)	AASB staff comment
subsequent measurement. The IASB also tentatively decided to clarify that, in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, an entity should select and apply its accounting policies consistently for similar contracts, considering the portfolio in which the contract is included, the assets that the entity holds and how those assets are accounted for. (This is in light of the tentative decision made at its March 2014 meeting, that an entity should choose to present the effect of changes in discount rates in profit and loss or in other OCI as its accounting policy and should apply that accounting policy to all contracts within a portfolio.)	**other than those measured using a premium allocation approach);** **is likely to cause insurers to recognise a significantly larger number of portfolios than they otherwise would if they were only required to group insurance contracts on the basis of similar risks. This is because insurers often identify and manage portfolios that comprise contracts with similar risks and have similar durations (a form of 'open' portfolio) rather than similar dates of inception.** Moreover, while the proposals may seemingly have the potential to increase comparability between insurers' portfolios, it is likely that the phrase 'similar dates of inception will garner a broad range of meanings in practice, thereby undermining any potential comparability benefits. By restricting the size of portfolios of insurance contracts in practice, the proposals are also likely to require insurers to apply the remeasurement proposals for short-duration insurance contracts in paragraph 60 of ED/2010/8 more frequently than they might otherwise.	