



Memorandum

To:	AASB members	Date:	2 December 2014
From:	Sue Lightfoot	Agenda Item:	15.1 (M142)
Subject:	Insurance Contracts: Consider Key Issues	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.

Attachments

Agenda Paper 15.2 Appendix to Agenda Paper 15.1: Previous IASB redeliberations on ED/2013/7 *Insurance Contracts* (AASB ED 244) [for information only].

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 submissions 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 (CSM);
- (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 tentative decisions made by the IASB on ED/2013/7 in its September 2014 meeting is given below. Comments and analysis regarding the March, April, May, June, July and September meetings are provided again for information purposes in the Appendix (Agenda Paper 15.2) to this memo.

As at the date of this memo, the IASB's tentative decisions are only in relation to contracts with no participating features. The IASB has indicated that its tentative decisions may be revisited at a later stage as a result of its consideration of participating contracts.

As agreed by the Board at its October 2014 meeting, AASB staff contacted IASB Board members (Darrel Scott and Ian Mackintosh) on 29 October 2014 to reconfirm the AASB's support for the IASB's tentative decision made in March 2014 that an entity should make an accounting policy choice to present changes in discount rates either in profit or loss or in OCI and apply that choice by portfolio. In that correspondence the staff also indicated that the support for profit or loss presentation is primarily driven by the view that the insurance liability measure is essentially a current value and that requiring a tracking back to inception-date discount rates is inconsistent with that current value. It was also noted that it is our view that the complexities that seem to come with the OCI presentation (especially for participating contracts) will inevitably lead to operational challenges (for both preparers and users) and that this could make profit or loss presentation attractive to a very wide group based on its relative simplicity.

October 2014

The IASB continued its discussion on initial application for insurance contracts with no participating features and made a number of tentative decisions. Refer to the table below for the staff analyses.

November 2014

At this meeting, the IASB held an education session in which representatives of the European CFO Forum presented their alternative proposals for the accounting for contracts with participating features. Those proposals are described in a paper prepared by the European CFO Forum attached to the November IASB Board papers.

No tentative decisions were made by the IASB in this meeting.

The alternative model is scheduled for discussion at the Asian-Oceanian Standards Setters Group meeting on 26-27 November 2014 and at the Accounting Standards Advisory Forum Meeting on 4-5 December 2014. Staff will provide a verbal update at the December AASB Board meeting.

Next steps

The IASB will continue its redeliberations in 2015. IASB staff expect that redeliberations of the proposals will be completed in the first half of 2015, with the publication of a final IFRS in late 2015.

Staff recommendation

Staff consider that there are no further issues to raise 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 October 2014 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
<i>October 2014</i>		
Initial application for contracts with no participating features		
<p>The IASB tentatively decided to confirm the 2013 Exposure Draft Insurance Contracts (2013 ED) proposals that at the beginning of the earliest period presented:</p> <p>(a) an entity should apply the Standard retrospectively in accordance with IAS 8 <i>Accounting Policies, Changes in Accounting Estimates and Errors</i> unless impracticable.</p> <p>(b) if retrospective application of the Standard is impracticable, an entity should apply the simplified approach proposed in paragraphs C5 and C6 of the 2013 ED with the following modification: instead of estimating the risk adjustment at the date of initial recognition as the risk adjustment at the beginning of the earliest period presented, an entity should estimate the risk adjustment at the date of initial recognition by adjusting the risk adjustment at the beginning of the earliest period presented by the assumed release of the risk before the beginning of the earliest period presented. The assumed release of risk should be determined by reference to release of risk for similar insurance contracts that the entity issues at the beginning of the earliest period presented.</p>	<p><i>Retrospective application</i></p> <p>5.1 The AASB supports the proposed transitional arrangements on the grounds that they would provide users with more relevant and useful information than the previous proposals in ED/2010/8 which would have resulted in no CSM being recognised for contracts in force at the beginning of the earliest period presented. Although these proposals are likely to result in significant costs being borne by preparers, the AASB expects that the resulting benefit would be likely to exceed those costs.</p> <p>5.2 The AASB has also identified a number of operational concerns in respect of retrospective application of the proposals, including:</p> <ul style="list-style-type: none"> determining appropriate historical discount rates, in particular, for long-dated insurance contracts. This would be alleviated if the use of historical rates is not required 	<p>The AASB supported the 2013 ED proposals to apply the requirements retrospectively on transition.</p> <p>AASB staff support the modification in respect of when retrospective application is impracticable, to estimate the risk adjustment by the assumed release of risk before the earliest period presented.</p> <p>AASB staff also support the additional fair value approach if the simplified approach is impracticable.</p> <p>The staff views on transition arrangements are consistent with the AASB's 2013 ED response to the IASB, which noted: "The AASB supports the IASB in seeking to formulate a common comprehensive IFRS. However, in doing so, the IASB needs to be mindful of the different starting points of each relevant jurisdiction."</p> <p>Staff support the IASB's tentative decision on disclosures for contracts for which the simplified or fair value approach is used. The additional disclosures specified in paragraph</p>

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IASB Tentative Decisions	Comment from AASB Submission to IASB (emphasis added in bold)	AASB staff comment
<p>The IASB also tentatively decided that:</p> <p>(a) if the simplified approach described in paragraph (b) above is impracticable, an entity should apply a fair value approach in which the entity should:</p> <p style="padding-left: 20px;">(i) determine the contractual service margin at the beginning of the earliest period presented as the difference between the fair value of the insurance contract at that date and the fulfilment cash flows measured at that date; and</p> <p style="padding-left: 20px;">(ii) determine interest expense in profit or loss, and the related amount of other comprehensive income accumulated in equity, by estimating the discount rate at the date of initial recognition using the method in the simplified approach proposed in paragraphs C6(c) and (d) of the 2013 ED.</p> <p>(b) for each period presented for which there are contracts that were measured in accordance with the simplified approach or the fair value approach, an entity should disclose the information proposed in paragraph C8 of the 2013 ED (ie the disclosures for contracts for which retrospective application is impracticable) separately for:</p> <p style="padding-left: 20px;">(i) contracts measured using the simplified approach; and</p> <p style="padding-left: 20px;">(ii) contracts measured using the fair value approach.</p>	<ul style="list-style-type: none"> • retrospective application of mirroring. This would also be somewhat alleviated if the use of OCI is not required. 	<p>C8 of the 2013 ED are:</p> <p>(a) the earliest date of initial recognition of the portfolios for which the entity applied this [draft] Standard retrospectively; and</p> <p>(b) the disclosures required by paragraphs 83–85 separately for portfolios to which paragraphs C3–C6 apply. At a minimum, an entity shall provide those disclosures for:</p> <p style="padding-left: 20px;">(i) the contractual service margin as determined in accordance with paragraphs C5–C6, including a description of the extent to which the entity used information that is not objective in determining that margin; and</p> <p style="padding-left: 20px;">(ii) the discount rates as determined in accordance with paragraph C6.</p> <p>[In respect of the concerns in paragraph 5.2:</p> <ul style="list-style-type: none"> • The concern about tracking has previously been communicated to the IASB and remains a concern. • The proposals in respect of ‘mirroring’ are in relation to participating contracts. The IASB is continuing its redeliberations on participating contracts and appears unlikely to pursue the mirroring approach.]