Accounting Standard

**AASB 1038**
November 1998

# Life Insurance Business

Issued by the
**Australian Accounting Standards Board**

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Defined words appear in *italics* the first time they appear in a section. The definitions are in Section 21. Standards are printed in **bold** type and commentary in light type.

# MAIN FEATURES OF THE STANDARD

The Standard:

(a) applies to life insurers and to the parent entities in economic entities that include a life insurer

(b) requires a life insurer and the parent entity of a life insurer to include in its financial report all its assets, liabilities, revenues, expenses and equity irrespective of whether they are designated as relating to policyholders or to shareholders

(c) requires all assets of a life insurer to be measured at net market values

(d) requires all liabilities of a life insurer to be measured at net present values, and describes the key parameters for measuring policy liabilities

(e) requires a life insurer that is a parent entity to recognise and disclose any excess (which will include any internally generated goodwill) or deficiency of the net market values of interests in subsidiaries over the net assets of those subsidiaries recognised in the consolidated financial report, in the financial report of the life insurer economic entity

(f) requires premiums and claims to be separated on a product basis into their revenue, expense and change in liability components unless the separation is not practicable or the components cannot be reliably measured, subject to a transitional provision

(g) requires returns on all investments controlled by a life insurer to be recognised as revenues

(h) requires participating benefits vested in relation to the financial year, other than transfers from unvested policyholder benefits liabilities, to be recognised as expenses

(i) requires reinsurance contracts to be recognised on a gross basis

(j) requires specific disclosures in the financial reports prepared by life insurers or economic entities which include a life insurer.

**ACCOUNTING STANDARD AASB 1038**

The Australian Accounting Standards Board makes Accounting Standard AASB 1038 "Life Insurance Business" under section 334 of the Corporations Law.

K H Spencer
Director – AASB

Dated 17 November 1998

# ACCOUNTING STANDARD

# AASB 1038 "LIFE INSURANCE BUSINESS"

## 1 Application

**1.1 This Standard applies to each *entity* that is:**

**(a) a *life insurer*; or**

**(b) the *parent entity* in an *economic entity* that includes a life insurer**

**and is required to prepare financial statements in accordance with Part 2M.3 of the Corporations Law and:**

**(c) is a *reporting entity*; or**

**(d) holds those financial statements out to be, or form part of, a *general purpose financial report*.**

1.1.1 This Standard applies to the consolidated financial report of an economic entity in relation to a life insurer *subsidiary*. Paragraph 5.2 is of particular relevance in these cases. This Standard does not apply to reporting by an economic entity for its activities other than its *life insurance business*. In measuring and reporting business other than life insurance business as well as aspects of life insurance business where this Standard contains no requirements, an economic entity that includes a life insurer should follow applicable accounting standards.

**1.2 In the event of a conflict between this Standard and any other Standard, the requirements of this Standard prevail.**

1.2.1 This Standard overrides the requirements of Accounting Standard AASB 1028 “Accounting for Employee Entitlements” in requiring all *liabilities* of life insurers to be measured at net present value.

1.2.2 This Standard requires all *assets* of life insurers to be measured at *net market value*. This requirement means that life insurers do not apply Standards that are predicated on the historical cost or modified historical cost bases of accounting. For this reason, for example, the use of net market values in measuring assets means that life insurers do not depreciate assets in accordance with Accounting Standard AASB 1021 “Depreciation”, revalue assets in accordance with Accounting Standard AASB 1010 “Accounting for the Revaluation of Non-Current Assets”, *recognise* and amortise goodwill in accordance with Accounting Standard AASB 1013 “Accounting for Goodwill”, recognise leases in accordance with AASB 1008 “Leases” and use the equity method of accounting in accordance with Accounting Standard AASB 1016 “Accounting for Investments in Associates”.

1.2.3 Accounting Standard AASB 1012 “Foreign Currency Translation” applies in relation to the translation of transactions, other than foreign currency hedge contracts, and foreign operations. Premiums received and claims paid in foreign currencies would need to be translated in accordance with AASB 1012. However, some of the requirements of AASB 1012 are not applicable where a net market value basis is used for measuring assets. The effect of movements in exchange rates on the carrying amounts of *investments* is included in their net market values, changes in which are recognised as part of investment *revenue* in the profit and loss statement as they occur. Because this applies in the case of foreign branch offices and where the investment is a foreign subsidiary, there is no recognition of a foreign currency translation reserve. The only case in which a foreign currency translation reserve would be recognised by a life insurer is in the context of its consolidated financial report where the reserve already exists in the financial report of a subsidiary which is not a life insurer.

# 2 Operative Date

**2.1 This Standard applies to *financial years* ending on or after 31 December 1999.**

**2.2 This Standard may be applied to financial years ending before 31 December 1999 where an election has been made in accordance with subsection 334(5) of the Corporations Law.**

2.2.1 Notice of this Standard was published in the *Commonwealth of Australia Gazette* on 19 November 1998.

# 3 Purpose of Standard

**3.1 The purpose of this Standard is to:**

**(a) prescribe the methods to be used for reporting on *life insurance business* in the financial report**

**(b) require disclosures about life insurance business in the financial report.**

# 4 Application of Materiality

4.1.1 The standards specified in this Standard apply to the financial report where information resulting from their application is material, in accordance with Accounting Standard AASB 1031 "Materiality". An example of the application of materiality is that disclosures about *life insurance business* in the context of an *economic entity* that includes a *life insurer* are required where the life insurance business is material in the context of the economic entity.

4.1.2 For the purposes of Accounting Standard AASB 1029 "Half-Year Accounts and Consolidated Accounts", the determination of policy liabilities in accordance with section 9 of this Standard does not necessarily require a full actuarial valuation. In accordance with AASB 1029, policy liabilities would need to be determined on a *reliable* basis, including a full review of assumptions, and not be materially different from policy liabilities determined by a full actuarial valuation.

# 5 Entity and Consolidation Issues

## The life insurer entity

**5.1 A *life insurer* must *recognise* in its financial report the *assets*, *liabilities*, *revenues*, *expenses* and *equity* of the *entity*, whether they are designated as relating to *policyholders* or to shareholders.**

5.1.1 Life insurers may have both policyholders and shareholders with a financial interest in the entity. It is sometimes argued that the interests of policyholders and the interests of shareholders form the bases of separate entities that should prepare separate primary financial reports. However, the view adopted in this Standard is that the interests of policyholders and shareholders are intertwined and form the basis of a single entity. The boundaries of this entity are defined by *control*. The directors of the life insurer, in pursuing its objectives, dominate the decision-making in relation to the financial and operating policies of the life insurer, which includes the assets of the entity, whether they are designated as relating to policyholders or to shareholders.

5.1.2 Equity in a shareholder-owned life insurer will generally comprise only shareholder equity. Although participants in the industry commonly refer to "policyholder retained profits", in relation to Australian business such amounts are unvested policyholder benefits liabilities. Under Australian legislation, "policyholder retained profits" relating to Australian *life insurance business* must be paid to policyholders, although the timing of the payment is at the discretion of the life insurer. A life insurer will only have policyholder equity if that life insurer has foreign life insurance operations in a jurisdiction that permits retained profits to remain unallocated between policyholders and shareholders, and the policyholders' component cannot be determined.

## Financial reports of economic entities that include a life insurer subsidiary

**5.2 The consolidated financial report of an *economic entity* that includes a life insurer *subsidiary* must recognise all of the assets, liabilities, revenues and expenses of that subsidiary, whether they are designated as relating to the policyholders or to the shareholders of that life insurer. The assets, liabilities, revenues and expenses of a life insurer subsidiary and its economic entity recognised in the consolidated financial report of an economic entity must be measured in accordance with this Standard.**

5.2.1 For the same reasons that a life insurer entity is considered to comprise both policyholder and shareholder interests, the view adopted in this Standard is that the *parent entity* controls the interests of both policyholders and shareholders and, accordingly, the consolidated financial report of the economic entity includes all of those interests. The parent entity of a life insurer effectively uses all of the resources of shareholders and policyholders in achieving its objectives and effectively controls policyholder interests for the benefit of both policyholders and shareholders.

5.2.2 Some life insurers are subsidiaries of entities other than life insurers, such as banks, and some are subsidiaries of other life insurers. The character of the parent entity of a life insurer has no bearing on whether consolidated financial reports, prepared in accordance with paragraph 5.2, are required.

## Consolidated financial reports of life insurers and investments in subsidiaries

**5.3 Any excess of the *net market values* of an interest in a subsidiary over the net amount of that subsidiary's assets and liabilities recognised in the consolidated financial report must be recognised in the consolidated financial report of a life insurer as a separate asset.**

5.3.1 These requirements reflect the life insurance industry's focus on the net market values of *investments*. In accordance with section 12 of this Standard, assets must be recognised in a life insurer's financial report at net market values. Some of these assets may be interests in subsidiaries. In a life insurer's consolidated financial report, the assets and liabilities relating to these interests may be recognised using the amounts in the records of the subsidiary. The net market value recognised in the life insurer's "parent entity" financial report may exceed the net amounts of the subsidiary's assets and liabilities. The "excess" may comprise the following components:

(a) acquired goodwill, to the extent that it remains at *reporting date*

(b) increments in the value of goodwill associated with a subsidiary since the acquisition or establishment of the subsidiary

(c) measurement differences, resulting from the assets and liabilities included in the life insurer economic entity financial report being carried in the records of a subsidiary on measurement bases other than those required in this Standard.

### Acquired goodwill

5.3.2 Under Accounting Standard AASB 1013 "Accounting for Goodwill", acquired goodwill, if any, is recognised on preparing economic entity financial reports and is amortised on a straight-line basis over its useful life. However, as indicated in paragraph 5.3.1(a), the separate asset required to be disclosed by paragraph 5.3 already includes any remaining acquired goodwill. Therefore, this Standard does not require either the separate recognition of acquired goodwill or its amortisation because it would not be relevant to separately recognise it once more on consolidation.

### Internally generated goodwill

5.3.3 The component noted in paragraph 5.3.1(b) is internally generated goodwill. This Standard overrides the requirements of AASB 1013, which prohibits the recognition of internally generated goodwill. The main reason noted in AASB 1013 for prohibiting the recognition of internally generated goodwill is the difficulty, or impossibility, of identifying the events or transactions which contribute to the overall goodwill of an entity. In addition, AASB 1013 notes that, even if these were identifiable, the extent to which they generate future benefits and the value of such benefits are not usually capable of *reliable* measurement.

5.3.4 Life insurers take an overall view of their subsidiaries as investments and may not attempt to assign particular values to underlying individual assets and liabilities. A reliable measure of net market value is used to determine the carrying amounts of whole businesses that are investments, with the increments and decrements in carrying amounts recognised as revenues and expenses as they occur. The effective recognition of internally generated goodwill relating to a subsidiary of a life insurer in the life insurer's financial reports is one of the facets of a net market value model.

5.3.5 In relation to the life insurance business conducted by the life insurer itself, internally generated goodwill is not recognised. This could only be possible where the interests of policyholders and the interests of shareholders form the bases of separate entities that prepare separate primary financial reports. As noted in paragraph 5.1.1, the view adopted in this Standard is that the interests of policyholders and shareholders are intertwined and form the basis of a single economic entity. Life insurers use the requirements of this Standard to report on their own life insurance business and would not, for example, use *embedded value* or *appraisal value* methods in relation to their own business. A parent entity which is not a life insurer may revalue its investment in a life insurer in the parent entity financial reports in accordance with Accounting Standard AASB 1010 "Accounting for the Revaluation of Non-Current Assets".

### Deficiency of net market values of interests in subsidiaries

**5.4 Any change in the deficiency of the net market values of a life insurer's interest in a subsidiary over the net amount of that subsidiary's assets and liabilities included in the consolidated financial report must be recognised in the consolidated financial report of the life insurer as a revenue or an expense only after:**

**(a) the carrying values of all assets and liabilities of the subsidiary have been reviewed, and remeasured where appropriate; and**

**(b) any asset recognised in accordance with paragraph 5.3 against which the deficiency must be offset has been eliminated.**

5.4.1 A deficiency of the net market value of a life insurer's interest in a subsidiary over the recognised net assets of that subsidiary may conceivably arise, although such a deficiency is expected to be extremely rare. Where such a rare circumstance arises, a life insurer parent entity should review the measurement of the net assets of the subsidiary to ensure that they are recognised and measured in accordance with the requirements of applicable accounting standards. If the subsidiary's net assets are over-valued, they should be remeasured. If the deficiency persists after a thorough and complete review, it is offset against any assets arising in respect of other subsidiaries as a result of applying the provisions of paragraph 5.3. The change in any remaining deficiency is recognised as a revenue or an expense in the financial report of the life insurer economic entity. The remaining deficiency is not recognised as a liability because it does not embody a present obligation.

## 6 Premiums and Claims

**6.1 Subject to paragraph 6.2, components of premiums that are *revenues* and components of claims that are *expenses* must be *recognised* separately in the profit and loss statement. Components of premiums that are not revenues and components of claims that are not expenses must be recognised as changes in policy liabilities.**

**6.2 For products where the separation of premiums and claims into components is not practicable or the components cannot be *reliably* measured, premiums must be recognised as revenues and claims must be recognised as expenses.**

6.2.1 A wide variety of products are offered by *life insurers* – risk products, *investment* products and numerous hybrids of these two products.

6.2.2 Traditionally, life insurers have treated all premiums as revenues and essentially all claims as expenses. However, premiums may comprise amounts that give rise to:

(a) revenues that are earned by providing services, including the bearing of risks

(b) amounts that are akin to deposits and which qualify for recognition as *liabilities*.

6.2.3 Similarly, claims may comprise amounts that give rise to:

(a) expenses that are incurred in providing services, including the bearing of risks

(b) amounts that are akin to withdrawals from deposits and which qualify for recognition as reductions in liabilities.

6.2.4 The performance of a life insurer is best reflected when only revenues and expenses are recognised in the profit and loss statement. The inclusion of other types of flows limits the ability of users to assess the performance of a life insurer's operations relative to other *entities* or investments.

6.2.5 The hybrid nature of many products and the sometimes complex manner in which fees are levied on *policyholder*s means that differentiating between the revenue and the liability components of premiums, and the expense and the liability components of claims, may be a difficult task and the costs involved may be significant. This is especially the case for *non-investment-linked business*. Notwithstanding the difficulties associated with reliably measuring the components of premiums and claims, for products where the components can be reliably measured the premiums and claims associated with those products are separately recognised as revenues, expenses and changes in policy liabilities for financial reporting purposes.

# 7 Reinsurance

## Substance of reinsurance contracts

**7.1 Reinsurance contracts must be accounted for as reinsurance in accordance with paragraphs 7.3 and 7.4 when and only when they provide for the transfer of risk against loss or *liability* from the ceding insurer to the reinsurer.**

**7.2 When a contract does not, despite its form, provide for the transfer of risk against loss or liability from the ceding insurer to the reinsurer, it must not be accounted for as reinsurance. The premium paid by the ceding insurer must be *recognised* as:**

**(a) an *asset* by the ceding insurer**

**(b) a liability by the reinsurer.**

7.2.1 A contract is not accounted for as reinsurance, regardless of its form, unless it provides for the transfer of risk from the ceding insurer to the reinsurer. This means, for example, that the amounts paid and received under a contract which provides for only an immaterial transfer of risk will be recognised as an asset by the ceding insurer and as a liability by the reinsurer. If a contract does not transfer risks from the ceding insurer to the reinsurer, a contract does not give rise to premiums that are *revenues* and claims that are *expenses*.

## Reporting by direct insurers

**7.3 A ceding insurer must recognise:**

**(a) premiums ceded to reinsurers as reinsurance expenses**

**(b) claim recoveries and commissions from reinsurers as revenues**

**(c) claim recoveries and other inflows not yet received from a reinsurer as an asset.**

7.3.1 *Life insurers* may reinsure some of their business. The direct life insurer remains responsible for the total amount of successful claims of *policyholders* and through reinsurance arrangements may be entitled to recover amounts relating to some of those claims.

7.3.2 Reinsurance contracts are considered to be separate transactions from the original life insurance policies and therefore give rise to separately recognisable amounts. The direct insurer recognises the gross amount of premiums received in accordance with paragraphs 6.1 and 6.2 and, where portions of the policies are reinsured, the ceded premiums are recognised as expenses. Any recoveries from reinsurers are recognised as revenues by the direct life insurer. Consistent with this approach, the gross amount of policy liabilities is recognised as a liability and claim recoveries not yet received from a reinsurer are recognised as a receivable by the direct insurer.

### Reporting by reinsurers

**7.4 Inwards reinsurance premiums and outwards reinsurance claims must be recognised by the accepting reinsurer as for premiums and claims in accordance with paragraphs 6.1 and 6.2. Policy liabilities assumed must be recognised as a liability by the accepting reinsurer in accordance with section 9.**

7.4.1 From the perspective of the reinsurer, reinsurance premiums accepted are recognised in the same way as the direct life insurer treats the acceptance of direct premiums. Correspondingly, claims paid and payable to direct insurers are recognised as expenses by the reinsurer. Consistent with these treatments, policy liabilities assumed are recognised as a liability by the accepting reinsurer.

## 8 Investment Revenues

**8.1 Returns on all *investments controlled* by a *life insurer* must be *recognised* as *revenues*.**

8.1.1 Interest, dividends, realised and unrealised capital gains and other returns on all the investments under the life insurer's control are revenues of the life insurer. This is the case whether the source of the investment returns are investments relating to premium revenues from *policyholders*, investments relating to inflows of deposits from policyholders or investments relating to funds received from shareholders. This treatment is consistent with the view that the life insurer controls the investments relating to both policyholders and shareholders and is responsible for investing them with the aim of maximising returns within risk constraints. In regard to the investments relating to policyholders, the life insurer has contracts with policyholders to pass on some or all of the investment returns based on the terms of the contracts. The investment returns related to the investments of both policyholders and shareholders are investment returns of the life insurer and, in turn, the life insurer will use those returns to meet its contractual obligations to policyholders.

# 9 Policy Liabilities

## Present value and best estimates

**9.1 Obligations arising from life insurance policies (policy liabilities) must be *recognised* as *liabilities* and must be measured at each *reporting date* as:**

**(a) the net present value of future receipts from and payments to *policyholders*, including participating benefits, allowing for the possibility of discontinuance before the end of policy contract periods, plus planned margins of *revenues* over *expenses* relating to services yet to be provided to policyholders, on the basis of assumptions that are best estimates; or**

**(b) where the result would not be materially different from the application of paragraph 9.1(a), the accumulated benefits to policyholders after allowing for the portion of *acquisition costs* expected to be recouped.**

9.1.1 The participating benefits component of policy liabilities includes previously vested benefits and future supportable bonuses. In addition to policy liabilities, there may be other liabilities that relate to participating policyholders. Policy benefits attributable to participating policyholders that are not yet vested with specific policyholders are recognised as liabilities. These are further discussed in section 11.

9.1.2 Premiums are generally received in advance of the provision of services to policyholders, including the payment of claims. In return for premiums, *life insurers* provide services, including the acceptance of risks, sometimes over long periods. Entering into a life insurance policy is considered to be the event that gives rise to future benefits and present obligations under a policy.

9.1.3 Where there are a number of variables relating to future uncertainties, a net present value approach to measuring policy liabilities is likely to provide the most appropriate measurement basis. The obligations under these more complex policies are generally measured as the present value of the expected inflows, such as premiums and fees, and outflows, such as claims and other expenses, based on assumptions relating to whole populations of policyholders, and taking into account applicable taxation.

9.1.4 An accumulation approach involves accruing the entitlements in policyholders' records at the reporting date. For example, in the case of an investment-linked policy, the life insurer could accrue the accumulated returns on the amount invested. If the fees expected to be charged by the life insurer to the policyholder in each future *financial year* are expected to equal or exceed any expenses incurred by the life insurer, the policy liability calculated under the accumulation approach would not be materially different from that obtained using the approach in paragraph 9.1(a).

9.1.5 The ultimate cost of meeting claims under many life insurance policies depends on the frequency of occurrence of particular future events such as death and surrender and other factors such as the future levels of *investment* returns, which are taken into account in setting discount rates. Assumptions need to be made about these future events. In order to ensure that policy liabilities are measured *reliably*, such assumptions need to be "best estimates".

9.1.6 Best estimate assumptions used in determining the present value of policy liabilities are made on the basis of the *assets* available to the life insurer at the reporting date and do not include any allowance for future contributions by owners and other funds which may be provided in the future to support the business.

9.1.7 Actuarial Standard AS 1.01 "Valuation of Policy Liabilities" issued by the Life Insurance Actuarial Standards Board provides guidance in the measurement of policy liabilities.

### Acquisition costs

9.1.8 Life insurance policies written in one financial year often give rise to benefits to the life insurer in subsequent financial years, such as future management fees and surrender penalties. Therefore, there are future benefits associated with the costs of acquiring life insurance policies, and such costs are often substantial.

9.1.9 Where relevant, in most industries acquisition costs are added to the carrying amounts of the assets acquired and subsequently amortised. In the life insurance industry, there is no reliable measure of the probable future economic benefits that will arise from acquisition costs. This is largely because of the uncertainty surrounding the continuance or surrender of particular policies. In practice, acquisition costs are usually recognised as expenses in the financial year in which they are incurred. This is generally offset by identifying a portion of the planned margins included in policy liabilities as relating to the recovery of acquisition costs. The most useful and reliable information available about the acquisition costs that will give rise to future economic benefits is the amount of future charges for acquisition costs identified as part of the process of determining policy liabilities.

## Recognition of planned margins as revenues

**9.2 Planned margins of revenues over expenses must be recognised in the profit and loss statement over the financial years during which the services to which those margins relate are provided to policyholders and the revenues relating to those services are received.**

9.2.1 In setting premium rates, life insurers will include planned margins of revenues over expenses. As noted in paragraph 9.1.2, premiums are generally received in advance of the provision of services to policyholders.

9.2.2 In this Standard, planned margins are recognised in the profit and loss statement when and only when the life insurer has performed the services necessary to establish a valid claim to those margins and has received the revenues relating to those services. To ensure that planned margins are recognised during the financial year in which the relevant services are provided, policy liabilities include a component relating to those margins. These margins are then "released" based on one or more factors or "profit carriers" which correspond to the performance of services and the earning of the margins. In relation to *investment-linked business*, the profit carrier might be maintenance expenses. In relation to many risk products, the profit carrier might be premiums or claims.

## Differences between actual and assumed experience

**9.3 Except in relation to investment earnings rate assumptions for *participating business*, the effect of changes in policy liabilities resulting from a difference between actual and assumed experience determined during the financial year must be recognised in the profit and loss statement as revenues or expenses in the financial year in which the changes occur.**

9.3.1 The assumed patterns and frequencies of events used in determining policy liabilities are compared with actual events in each financial year to assess their accuracy. The effects of differences between actual and assumed experience represents decreases or increases in the expected payments to policyholders and are revenues or expenses of the financial year in which the differences occur. For example, where the assumed costs of death claims under a renewable term life product line are greater than the actual costs for a financial year, a revenue equal to the difference is recognised in the profit and loss statement for the current financial year.

9.3.2 The recognition of the net amount of changes in policy liabilities resulting from a difference between actual and assumed experience identified during the financial year as a revenue or an expense is consistent with the use of assumptions that are best estimates as at each reporting date.

## Changes to underlying assumptions

**9.4 Assumptions used for measuring policy liabilities must be reviewed for each financial year. Where the review leads to changes in assumptions, with the exception of new business, the changes must be deemed to occur at the reporting date.**

9.4.1 Assumptions used for measuring new business may be deemed to have occurred at the beginning of the financial year, or at the date of commencement of the new business or at the end of the financial year.

9.4.2 In preparing interim financial reports, the reporting date is the interim reporting date. Accordingly, changes in assumptions are deemed to occur at the interim reporting date.

**9.5 The financial effects of changes to the assumptions underlying the measurement of policy liabilities made during the financial year must be recognised in the profit and loss statement over the future financial years during which services are provided to policyholders, except that:**

**(a) any estimated excess of the present value of future expenses over the present value of future revenues for a group of related products arising during the financial year must be recognised as an expense of the financial year**

**(b) the reversal of an expense previously recognised in accordance with sub-paragraph 9.5(a) must be recognised as a revenue of the financial year in which the reversal of the loss is recognised**

**(c) the effects of a change to assumed discount rates caused by changes in investment market conditions must be recognised as a revenue or an expense of the financial year in which the change occurs**

**(d) calculation errors and similar errors must be recognised as revenues or expenses in the financial year in which they are identified.**

9.5.1 The assumptions underlying the measurement of policy liabilities are reviewed at each reporting date. Based on past experience and revised expectations about the future, it may become apparent that particular assumptions are not consistent with likely future experience and need to be changed. Such changes are effectively a reassessment of the likely patterns and frequencies of future events. The normal revision of assumptions is not considered to be an error.

9.5.2 Apart from the circumstances identified in paragraph 9.5, changes to underlying assumptions are effectively recognised over future financial years by adjusting the planned margins included in policy liabilities. If the effect of a changed assumption is a decrease in the present value of present obligations to policyholders, the planned margin is increased. If the effect is an increase in the present value of obligations to policyholders, the planned margin is reduced. The overall amount of policy liabilities is not affected by these changes to underlying assumptions, as long as the planned margin of revenues over expenses is not eliminated.

### Losses on groups of related products

9.5.3 Situations may arise where the present value of the planned margin of revenues over expenses for a group of related products will be adjusted as a result of changing underlying assumptions to the extent that the planned margin is eliminated and becomes a planned loss. That is, the present value of estimated future expenses for a group of related products exceeds the present value of estimated future revenues. In such circumstances, the excess of the present value of expenses over revenues arising during the financial year is recognised in the profit and loss statement in the financial year in which the assessment is made. The loss reflects a higher present obligation due to adverse claims, which are now expected in future years. Whilst the claims giving rise to the loss are yet to occur, this treatment is justified on the basis that entering into life insurance policies is an event that gives rise to a present obligation to meet the expected future claims.

9.5.4 A group of related products would be products that have substantially the same contractual terms and were priced on the basis of substantially the same assumptions.

### Changes to discount rates

9.5.5 As with other assumptions, the discount rates used in determining policy liabilities are reviewed at each reporting date. Discount rates are based on currently expected rates of return on the assets supporting policy liabilities (refer to paragraph 9.6). However, unlike other assumptions, the effects of a change to assumed discount rates caused by changes in investment market conditions are recognised in the financial year in which the change is made. For a life insurer with a typical spread of investments, if market rates of return fall investment values generally rise and the resulting increases in investment values are recognised as revenues in the financial year in which they occur. Where the discount rates are adjusted in line with such falls in market rates, policy liabilities will increase and an expense will be recognised, having an offsetting (but not usually matching) effect on the increased investment values.

9.5.6 In relation to participating business (which is discussed at section 11), the effect of a change to the assumptions about discount rates, explained in paragraph 9.5.5, is a result of adjusting the best estimate of policy liabilities, including future participating benefits. For example, if market rates of return rise investment values generally fall and the resulting decreases in investment values are recognised as an expense in the financial year in which they occur. The fall in investment values will clearly impact on the ability of the life insurer to support future participating benefits. These are likely to be reduced, with an offsetting effect on the reduced investment values. The effect of an adjustment of the best estimate of future participating benefits included as a component of policy liabilities is the same as an adjustment of policy liabilities in the case of *non-participating business*.

### Discount rates

**9.6 The discount rates used in determining policy liabilities must be the currently expected after tax average rates for products that are taxed at the product level and the currently expected before tax average rates for products taxed on a profit basis. The discount rates must be based on market returns on investments supporting policy liabilities.**

9.6.1 Among the key assumptions underlying the present value measurement of policy liabilities are the discount rates used in discounting expected future cash flows. The most relevant amount of policy liabilities is the amount which is required as at the reporting date to meet a life insurer's policy obligations when they fall due. If policy liabilities are to represent expected cash flows, the discount rates used need to be based on the average returns on investments that are currently expected to arise and will contribute to discharging policy liabilities. The discount rates would relate to the total expected yields on investments and would therefore comprise what are sometimes described as income and capital gains.

## 10 Other Liabilities

**10.1 Other *liabilities* must be measured at net present values as at *reporting date*. Any changes in the net present values must be *recognised* in the profit and loss statement as *revenues* or *expenses* in the *financial year* in which the changes occur.**

10.1.1 This Standard requires that policy liabilities are measured at net present values and *assets* are measured at *net market values*. It is consistent to also measure other liabilities, including subordinated debt, at net present values using discount rates that reflect current market conditions for the liabilities concerned. That is, for example, a changed market yield for a long-term debt would result in a changed amount being recognised as a liability in the balance sheet and in a revenue or an expense being recognised in the profit and loss statement. It should be noted that where other liabilities are immaterial, they could be measured on a cost basis without contravening this Standard.

## 11 Participating Benefits

**11.1 Except for transfers from unvested policyholder benefits liabilities, participating benefits vested in *policyholders* in relation to the *financial year* must be *recognised* in the profit and loss statement as *expenses* for the financial year. Such benefits which remain payable as at the *reporting date* must be recognised as a component of policy liabilities.**

**11.2 Participating benefits that have been allocated in relation to the financial year to participating policyholders generally, but that have not yet vested in specific policyholders, must be recognised as expenses for the financial year. Amounts that have been**

**allocated to participating policyholders generally, but that have not vested in specific policyholders as at the reporting date, must be recognised as unvested policyholder benefits liabilities.**

11.2.1 Some *life insurers* sell *participating business*. Participating policyholders are generally eligible to receive the same types of benefits as other policyholders and, in addition, are entitled to participate in the profits relating to participating business. For example, a participating policyholder may receive a low contractually determined rate of return on savings together with term life cover and, in addition, receive benefits that depend on the *investment* performance of the pool of *assets* associated with participating policies and on the risk experience of participating policyholders. These additional benefits are often called bonuses and are at the discretion of the life insurer. In some financial years the life insurer may withhold a portion of the "profits" from the pool of participating business and recognise these "profits" as unvested policyholder benefits liabilities. In other financial years the life insurer may "top up" the vested benefits to participating policyholders. Such vesting of benefits is often done to provide a reasonably level vesting of benefits over time, despite volatility in periodic profits from participating business.

11.2.2 It is sometimes argued that the discretionary nature of participating benefits means that they should be treated as appropriations of profit in the same way as dividends to shareholders. Because policy liabilities relating to all types of policyholders are recognised as *liabilities*, it is appropriate for the participating benefits vested in relation to the financial year, other than transfers from unvested policyholder benefits liabilities, to be recognised as expenses of the financial year.

11.2.3 Mutual life insurers are effectively owned by their policyholder members. Nevertheless, the mutual life insurer also has obligations to its policyholders. These obligations are classified as policy liabilities. Benefits vested in a mutual life insurer's policyholders, other than transfers from unvested policyholder benefits liabilities, are also to be recognised as expenses in the financial year in which they are vested.

11.2.4 For financial reporting purposes, participating benefits vested in policyholders in a financial year but not yet paid are included in policy liabilities and are measured at net present values. In the case of investment account participating business this may be approximately the same as the amount actually allocated to policyholder accounts. In the case of traditional participating business, there may be a significant difference between the net present value and the face value of the amount vested in policyholders. The net present value is relevant for financial reporting purposes because it is the best estimate of the net present value of the amount that the life insurer expects to pay out in the future using information of experience up to the reporting date.

11.2.5 Where a life insurer "tops up" the vested benefits from previously recognised unvested policyholder benefits liabilities, a transfer between liabilities is recognised. If a life insurer tops up the vested benefits for participating policyholders other than from unvested policyholder benefits liabilities, the amount of the "top up" is recognised as an expense of the financial year in which the additional benefits are vested.

# 12 Assets

## Measurement

**12.1 *Assets* of a *life insurer* must be measured at *net market values* as at *reporting date*. Any changes in the net market values must be *recognised* in the profit and loss statement as *revenues* or *expenses* in the *financial year* in which the changes occur. For assets without active and liquid markets, the methods used to determine their net market values must be disclosed.**

12.1.1 The assets of a life insurer will typically comprise:

(a) *investments*, including investments in *subsidiaries*

(b) operating assets, such as fixtures and fittings

(c) accounts receivable

(d) cash.

12.1.2 In determining net market values of investments, reference is made to the market that provides the most *reliable* information, which is likely to be the market in which the investment is normally traded. In addition, whilst investments are often managed in the context of portfolios, they are nonetheless measured individually.

12.1.3 For many assets, such as *equity* securities of major listed *companies*, quoted market prices provide a reliable measure of net market value at reporting date. However, in some cases, it may be difficult to reliably measure the net market value of an asset. For example, in the case of a shareholding in a private company there may not be an active and liquid market for the shares. In such circumstances, the life insurer would make its best estimate of the net market value of that asset, taking into account all available information. In the case of material classes of assets, disclosure of the methods used in determining the net market values are relevant to users of the financial reports in assessing the financial performance and financial position of the life insurer.

12.1.4 In accordance with paragraph 12.1, a *parent entity* that is a life insurer would classify its interests in *controlled entities*, including any life insurer subsidiaries, as investments and measure them at net market value.

12.1.5 It is sometimes argued that a distinction should be made between investment and operating assets of life insurers for measurement purposes. Under this view, investments would be measured at net market values whilst operating assets would be measured in accordance with Accounting Standards AASB 1010 "Accounting for the Revaluation of Non-Current Assets" and AASB 1021 "Depreciation".

12.1.6 Any distinction between investment and operating assets is arbitrary because all assets of a life insurer contribute to generating returns to satisfy *policyholder* and shareholder expectations. The use of net market values and the recognition of all changes in values as revenues and expenses provide relevant information to users about the resources available to policyholders and shareholders and the life insurer's performance in deploying those assets. Where operating assets are immaterial, they could be measured on a cost basis without contravening this Standard.

## Recognition

**12.2 A life insurer must not recognise the excess of its own *embedded value* over its recognised net assets as an asset.**

12.2.1 Although section 5 requires that a life insurer recognise a subsidiary at market value in both the "parent" and *economic entity* financial reports, this Standard prohibits a life insurer from recognising the excess of its own embedded value over its other recognised net assets in its financial statements.

# 13 Imputed Inflows and Outflows

**13.1 Subject to paragraph 18.3, a *life insurer* must *recognise* imputed inflows and outflows as *revenues* and *expenses* when and only when such imputed flows relate to transactions with external *entities*.**

13.1.1 Life insurers often impute inflows and outflows to different classes of *policyholders* in order to help ensure that they are treated equitably. For example, a life insurer may own the buildings that it occupies. The funds of a particular group of policyholders are used to acquire and operate such buildings whilst a wider group of policyholders and shareholders may benefit from the use of the buildings. In the owner-occupied building example, the life insurer imputes an inflow of rent income to the policyholders whose funds are used to acquire and operate the buildings and imputes an outflow of rent cost to the other policyholders and to shareholders.

13.1.2 In cases where there are no transactions with external entities, such as with owner-occupied buildings, the life insurer is dealing with itself. There is no transaction or other past event that gives rise to a revenue or an expense. Any inflows and outflows imputed for internal management purposes would be eliminated in preparing external financial reports except in relation to the disaggregated disclosures required by paragraphs 18.1 and 18.2.

13.1.3 In some cases, life insurers impute inflows and outflows where external entities are involved. For example, life insurers often lend funds to their employees at concessional rates of interest with the funds being provided by a particular group of policyholders, whilst other policyholders and any shareholders benefit from the services provided by those employees. Because external parties are involved, such imputed inflows and outflows are recognised as revenues and expenses when they can be *reliably* measured.

# 14 Income Tax

## Application of income tax Standard

**14.1 *Life insurers* must account for income tax in accordance with Accounting Standard AASB 1020 "Accounting for Income Tax (Tax-effect Accounting)", except that:**

**(a)** **tax *assets* and *liabilities* must be measured at present values; and**

**(b)** **disclosures about permanent differences or a reconciliation between income tax *expense* (*revenue*) and income tax calculated as the current income tax rate applied to the profit or loss from ordinary activities before income tax expense are not required.**

14.1.1 It is important for life insurers to maintain equity between existing *policyholders* and between policyholders over time. This is reflected in the financial report through the use of current value methods of measurement.

14.1.2 Liabilities are generally measured at net present values and assets are measured at *net market values*, which reflect net present values. It is consistent for life insurers to also measure tax assets and liabilities at present values. Tax assets and liabilities will effectively be at present values where they are determined on the basis of tax effects on liabilities and assets that are measured at net present values or net market values. However, the timing of the relevant tax cash flows may need to be examined to determine whether any adjustments are needed. In addition, the discount rates used to determine the present values of tax assets and liabilities may need to be different from the rates used for other assets and liabilities because the risks pertaining to tax-related cash flows are different from the risks associated with other cash flows.

14.1.3 AASB 1020 requires disclosure of the nature and extent of any material permanent differences. The income tax payable by a life insurer is determined on a basis that is not derived from its operating results and income tax expense is determined at different rates for different classes of business. Accordingly, detailed disclosures about the nature and extent of any permanent differences are not useful to users of the financial report.

## Disclosures

**14.2** **The financial report must include a brief description of the income tax regime applying to the life insurer and disclose the basis on which the carrying amounts of tax assets and liabilities have been determined.**

14.2.1 Life insurance activities are taxed in various ways, usually dependent on the nature of the product involved. The forms and rates of tax are often different from those applying in other industries and information about the tax regime under which each life insurer operates is useful to users of financial reports.

## 15 Financial Performance Disclosures

**15.1 The following *revenues* and related explanations must be disclosed:**

**(a) premium revenue**

**(b) the accounting policy adopted in *recognising* premium revenue**

**(c) inwards reinsurance revenues**

**(d) *investment* revenue, showing separately revenue from:**

**(i) *equity* securities**

**(ii) debt securities**

**(iii) properties**

**(iv) other**

**(e) revenue arising from the recognition of a deficiency of the *net market values* of interests in *subsidiaries* over the net amount of subsidiaries' *assets* and *liabilities*, in accordance with paragraph 5.4**

**(f) other revenue.**

15.1.1 In accordance with the principles embodied in this Standard, with the exception of premium revenue recognised in accordance with paragraph 6.1, all revenues are to be recognised and disclosed before the effects of any transfers to or from policy liabilities. Disclosure of the effects of transfers to and from policy liabilities is required by section 15.5.

15.1.2 Investment revenues are shown in four categories, and the amount in each category would potentially include amounts received, amounts receivable and realised and unrealised gains and losses relating to the *financial year*. That is, for example, the category "investment revenues from equity securities" would include dividends received and receivable relating to the financial year, realised gains and losses from trading during the financial year and unrealised gains and losses from holding equity securities during the financial year.

**15.2 The following *expenses* and related explanations must be disclosed:**

**(a) outwards reinsurance expense**

**(b) operating expenses, showing separately:**

**(i) claims expense**

**(ii) policy acquisition expenses, separated into material components including commission**

**(iii) policy maintenance expenses**

**(iv) investment management expenses**

**(v) other**

**(c) the accounting policy adopted in recognising claims expense**

**(d) the basis for the apportionment of operating expenses between policy acquisition, policy maintenance and investment management expenses**

**(e) any expense arising from the recognition of a deficiency of the net market values of interests in subsidiaries over the net amount of subsidiaries' assets and liabilities, in accordance with paragraph 5.4.**

15.2.1 In accordance with the principles embodied in this Standard, with the exception of claims expense recognised in accordance with paragraph 6.1, all expenses are to be recognised and disclosed before the effects of any transfers to or from policy liabilities. Disclosure of the effects of transfers to and from policy liabilities is required by section 15.5.

**15.3 Where any premiums and any claims are separated into their revenue, expense and change in liability components in accordance with paragraph 6.1, total premiums and total claims must be disclosed.**

15.3.1 The mix of products written by a *life insurer* will vary between life insurers. In addition, different life insurers will find that the separation of premiums and claims into their components is practicable for different products. Comparability between life insurers is enhanced by the disclosure of total premiums and total claims.

**15.4 Where a profit is recognised at the inception of a group of policies, the revenues and expenses associated with that group of related products must be disclosed in the financial year in which those policies were written.**

15.4.1 It is expected that profit will be recognised at the inception of a policy only on rare occasions. It is considered that this profit is of such an incidence that it should be disclosed.

**15.5 The following components of operating profit after income tax expense must be shown, separated between *policyholder* and shareholder interests:**

**(a) profit related to movements in policy liabilities, separated between:**

**(i) planned margins of revenues over expenses**

**(ii) the difference between actual and assumed experience**

**(iii) the effects of changes to underlying assumptions**

**(iv) loss recognition on groups of related products or reversal of previously recognised losses**

**(v) other movements, separated into material components**

**(b) investment earnings on assets in excess of policy liabilities**

**(c) other items, separated into material components.**

## Other disclosures

15.5.1 Accounting Standards and the *Life Insurance Act 1995* differ in their treatment of participating benefits. Accordingly, life insurers are encouraged to disclose a reconciliation between:

(a) the profit for the financial year reported under Accounting Standards and the profit for the financial year reported under the *Life Insurance Act 1995*

(b) the retained profits at the end of the financial year reported under Accounting Standards and the retained profits at the end of the financial year reported under the *Life Insurance Act 1995*.

15.5.2 This Standard prescribes disclosure requirements specific to *life insurance business*. Other Accounting Standards prescribe disclosure requirements for all *reporting entities*, including life insurers.

# 16 Financial Position Disclosures

## Assets

**16.1 The following *assets* must be disclosed in the broad order of their liquidity:**

**(a) *investments*, showing separately:**

**(i) *equity* securities**

**(ii) debt securities**

**(iii) properties**

**(iv) other, by major class where applicable**

**(b) operating assets**

**(c) reinsurance recoveries receivable**

**(d) any excess net market value asset *recognised* in accordance with paragraph 5.3, together with the components disaggregated by *subsidiary*, and explanations of:**

**(i) the factors giving rise to that asset; and**

**(ii) any changes in that asset from the previous *financial year*.**

### Liquidity ranking

16.1.1 The presentation of assets and *liabilities* in the broad order of their liquidity is considered to be relevant to emphasise the importance of liquidity and solvency for *life insurers*. The current/non-current presentation of assets and liabilities is not considered to give rise to sufficiently useful information for users.

### Investments

16.1.2 Disclosures about the different types of investments and investment *revenues* provide users with information that assists them in understanding the nature and extent of the risks and returns associated with the investments held by a life insurer. Accordingly, investments are shown in classes that reflect their underlying nature. For example, units held in a property trust are classified as a property investment.

16.1.3 Some types of land and buildings may be investments that are also used in the operation of the *life insurance business*. An example is office buildings owned and occupied by a life insurer. The predominant purpose in holding all types of land and buildings in the context of a life insurance business is the generation of investment returns. Accordingly, these assets are classified as investments.

### Measurement methods

16.1.4 Paragraph 12.1 requires assets to be measured at *net market values* as at *reporting date*, and that where assets are without active and liquid markets, the methods used to determine their net market values are to be disclosed.

### Other disclosures

16.1.5 This Standard requires minimum disclosures and it is likely that, in many cases, more extensive disclosures would be appropriate. For example, in relation to investment properties it may be useful to disclose separately the extent of holdings in the commercial/retail, industrial, rural, and residential sectors.

### Restrictions on assets

**16.2 Restrictions attaching to assets held for the benefit of *policyholders* must be disclosed.**

16.2.1 There are a number of restrictions on the use of assets invested for policyholders in *life funds*. It is important that these restrictions be disclosed so that users of the financial report can assess their impact.

## Liabilities

**16.3 Policy liabilities, unvested policyholder benefits liabilities and other liabilities, classified by nature, must be disclosed in the broad order of their liquidity. The following components of policy liabilities must also be disclosed:**

**(a) future policy benefits, including participating benefits**

**(b) balance of future *expenses***

**(c) planned margins of revenues over expenses**

**(d) future charges for *acquisition costs***

**(e) balance of future revenues**

**(f) other items, separated into material components.**

## Acquisition costs

16.3.1 In the life insurance industry, unlike other industries, acquisition costs are not recognised as an asset because there is no *reliable* measure of the probable future economic benefits that will arise from actual acquisition costs. In practice, acquisition costs are usually recognised as expenses in the financial year in which they are incurred. This is generally offset by identifying a portion of the planned margins included in policy liabilities as relating to the recovery of acquisition costs. The most useful and reliable information available about the acquisition costs that will give rise to future economic benefits is the amount of future charges for acquisition costs identified as part of the process of determining policy liabilities. Disclosure of this amount is required under paragraph 16.3(d).

## Guaranteed or assured returns of funds invested

**16.4 The amount of policy liabilities which relates to guaranteed or assured returns of funds invested must be disclosed.**

16.4.1 Many life insurers sell life insurance policies that provide some form of guarantee or assurance about the return of funds invested. It is useful for users of life insurers' financial reports to have information about the extent of such guarantees or assurances, since they involve the life insurer bearing investment risks on behalf of policyholders.

## Equity

**16.5 The following components of equity must be disclosed:**

**(a) retained profits wholly attributable to shareholders**

**(b) retained profits where the allocation between participating policyholders and shareholders cannot be determined.**

16.5.1 Information about the different components of retained profits is useful in meeting the accountability obligations of the life insurer for the whole business and in showing the relative positions of the major stakeholders.

16.5.2 A life insurer that has sold *participating business* may have "retained profits" generated from that business. In relation to Australian participating policyholders, these "retained profits" are liabilities which are disclosed separately from policy liabilities in accordance with paragraph 16.3. In foreign life insurance operations, retained profits may exist which have yet to be allocated between policyholders and shareholders. Such retained profits are separately disclosed. It is relevant to note that retained profits directly attributable to shareholders may reside in both life funds and a shareholder fund.

## Solvency information

**16.6 A life insurer must disclose the solvency position of each life fund. An *economic entity* must disclose the solvency position of each life insurer in the economic entity.**

16.6.1 Under the *Life Insurance Act 1995*, life insurers are required to hold reserves in excess of the amount of policy liabilities. These additional reserves are necessary to support the life insurer's capital requirements under its business plan and to provide a cushion against adverse experience in managing long-term risks. The Life Insurance Actuarial Standards Board has issued Actuarial Standard 2.01 "Solvency Standard" for determining the level of solvency reserves. Because solvency is an important aspect of a life insurer's financial position, information about it is useful to users of financial reports.

### Managed funds and other fiduciary activities

**16.7 The nature and amount of the life insurer's activities relating to managed funds and trust activities, and whether arrangements exist to ensure that such activities are managed independently from its other activities, must be disclosed.**

## 17 Actuarial Information

**17.1 The following must be disclosed in notes to the financial statements:**

**(a) if other than the *reporting date*, the effective date of the actuarial report on policy liabilities and solvency reserves**

**(b) the name and qualifications of the actuary**

**(c) whether the amount of policy liabilities has been determined in accordance with the requirements of the *Life Insurance Act 1995***

**(d) whether the actuary is satisfied as to the accuracy of the data from which the amount of policy liabilities has been determined.**

### Disclosure of assumptions

**17.2 A summary of the key assumptions used in determining policy liabilities must be disclosed in notes to the financial statements, including:**

**(a) discount rates, *asset* mix, and inflation rates**

**(b) profit carriers used for each major product group**

**(c) future maintenance and *investment* management *expenses*, the rate of inflation applicable to them and any automatic indexation of benefits and premiums**

**(d) rates of taxation**

**(e) mortality and morbidity, by reference to the identity of the tables**

**(f) rates of discontinuance**

**(g) the basis of calculating surrender values**

**(h) rates of growth of unit prices in respect of unit-linked benefits**

**(i) rates of future supportable participating benefits**

**(j) the crediting policy adopted in determining future supportable participating benefits and how it compares with the *life insurer's* actual practice.**

# 18 Disaggregated Information

## Life funds and the shareholder fund

**18.1 For each *life fund* and for the shareholder fund, the following must be disclosed:**

**(a) *investment assets***

**(b) other assets**

**(c) policy liabilities**

**(d) *liabilities* other than policy liabilities**

**(e) retained profits, showing the amount directly attributable to shareholders and other retained profits**

**(f) premium *revenue***

**(g) investment revenue**

**(h) claims *expense***

**(i) other operating expenses**

**(j) investment revenues paid or allocated to *policyholders***

**(k) operating profit (loss) before tax**

**(l) operating profit (loss) after tax**

**(m) transfers to or from other funds.**

18.1.1 Disaggregated information for each life fund and the shareholder fund is useful because, under Australian legislation, each *life insurer* may have more than one fund and, in general, the assets of each life fund are only available to meet the liabilities and expenses of that life fund.

## Investment-linked and non-investment-linked business

**18.2 A life insurer must disclose the information required by sub-paragraph 18.1(a) to (l) disaggregated between those amounts relating to *investment-linked business* and those relating to *non-investment-linked business*.**

18.2.1 The risks and potential rewards for a life insurer differ substantially as between investment-linked business and non-investment-linked business. Accordingly, disaggregated information about these is considered to be useful in assessing the financial performance and financial position of a life insurer. The information required by paragraph 18.2 is for the *entity's life insurance business* as a whole. It is not required for each life fund.

## Geographical segments

18.2.2 Further disaggregated information may be required by Accounting Standard AASB 1005 "Financial Reporting by Segments".

## Imputed inflows and outflows

**18.3 Disclosures required by paragraphs 18.1 and 18.2 must include all imputed inflows and outflows as revenues and expenses where they can be *reliably* measured.**

18.3.1 As discussed in paragraph 13.1.1, life insurers often impute inflows and outflows to different classes of policyholders and shareholders to help ensure that they are treated equitably. Whereas, in relation to the profit and loss statement and the balance sheet, paragraph 13.1 only permits the *recognition* of imputed inflows and outflows relating to transactions with external parties, paragraph 18.3 requires all imputed inflows and outflows to be included in the disaggregated information to reflect the performance of each segment of the life insurer.

## 19 Comparative Information

**19.1 Information for the preceding corresponding *financial year* which corresponds to the disclosures specified for the current financial year must be disclosed, except in respect of the following:**

**(a) the financial report of a *life insurer* or the *parent entity* of an *economic entity* containing a life insurer for the first financial year to which this Standard is first applied, if impracticable; or**

**(b) the first consolidated financial report of a life insurer after it becomes a parent entity; or**

**(c) the first consolidated financial report of an *entity* other than a life insurer after it becomes a parent of a life insurer.**

## 20 Transitional Provisions

**20.1 Where the accounting policies required by this Standard are not already being applied as at the beginning of the *financial year* to which this Standard is first applied, they must be applied at that date. Where this gives rise to initial adjustments which would otherwise be *recognised* in the profit and loss statement, the net amount of those adjustments, including any adjustments to income tax *assets* and *liabilities*, must, in accordance with Accounting Standard AASB 1018 "Profit and Loss Accounts", be adjusted against retained profits or accumulated losses as at the beginning of the financial year to which this Standard is first applied.**

**20.2 All premiums and claims may be disclosed as if they are all *revenues* and *expenses* until the first financial year ending on or after 31 December 2001.**

20.2.1 The transitional provision in paragraph 20.2 affects the recognition requirements of paragraphs 6.1 and 6.2 and the disclosure requirements of paragraphs 15.1(a), 15.2(b)(i) and 15.3.

**20.3 Any asset revaluation reserve recognised in the financial statements of a *life insurer* prior to the application of this Standard must be transferred directly to retained profits or**

**accumulated losses as at the beginning of the financial year to which this Standard is first applied.**

## 21 Definitions

**21.1 In this Standard:**

***acquisition costs*** **means the fixed and variable costs of acquiring new business, including commissions and similar distribution costs, and costs of accepting, issuing and initially recording policies**

***appraisal value*** **means the *embedded value* of a *life insurer* together with the present value of expected profits from future new business**

***assets*** **means future economic benefits *controlled* by the *entity* as a result of past transactions or other past events**

***borrowing corporation*** **is defined in the Corporations Law**

***company*** **is defined in the Corporations Law**

***control*** **means the capacity of an entity to dominate decision-making, directly or indirectly, in relation to the financial and operating policies of another entity so as to enable that other entity to operate with it in pursuing the objectives of the controlling entity**

***economic entity*** **means a group of entities comprising the *parent entity* and each of its *subsidiaries***

***embedded value*** **means the net present value of the shareholders' entitlements from existing *assets* and future cash flows from life insurance policies in force at the *reporting date***

***entity*** **means any legal, administrative, or fiduciary arrangement, organisational structure or other party (including a person) having the capacity to deploy scarce resources in order to achieve objectives**

***equity*** **means the residual interest in the assets of the entity after deduction of its *liabilities***

***expenses*** **means consumptions or losses of future economic benefits in the form of reductions in assets or increases in liabilities of the entity, other than those relating to distributions to owners, that result in a decrease in *equity* during the *financial year***

***financial year*** **is defined in the Corporations Law**

***general purpose financial report*** **means a financial report intended to meet the information needs common to users who are unable to command the preparation of reports tailored so as to satisfy, specifically, all of their information needs**

***holding company*** **is defined in the Corporations Law**

***investment*** **means an asset held by the entity for the accretion of wealth by way of *revenues* such as interest, royalties, dividends, rentals and capital appreciation, but does not include operating assets**

***investment-linked business*** **means business for which the life insurer issues a contract where the benefit amount is directly linked to the market value of the *investments* held in the particular investment-linked fund**

***liabilities*** **means future sacrifices of economic benefits that the entity is presently obliged to make to other entities as a result of past transactions or other past events**

***life fund*** **means a statutory fund under the *Life Insurance Act 1995***

***life insurance business*** **means all business conducted by a life insurer**

***life insurer*** **means an entity registered under the *Life Insurance Act 1995* and similar entities operating outside Australia**

***listed corporation*** **is defined in the Corporations Law**

***net market value*** **means the amount which could be expected to be received from the disposal of an asset in an orderly market after deducting costs expected to be incurred in realising the proceeds of such a disposal**

***non-investment-linked business*** **means *life insurance business* other than *investment-linked business***

***non-participating business*** **means life insurance business that consists of the provision of non-participating benefits under life insurance policies**

***parent entity*** **means an entity which controls another entity**

***participating business*** **means life insurance business that consists of the provision of participating benefits under life insurance policies**

***policyholders*** **means *policy owners***

***policy owners*** **is defined in the *Life Insurance Act 1995***

***recognised*** **means reported on, or incorporated in amounts reported on, the face of the profit and loss statement or of the balance sheet (whether or not further disclosure of the item is made in notes)**

***reliability*** **means that quality of financial information which exists when that information can be depended upon to represent faithfully, and without bias or undue error, the transactions or other events that either it purports to represent or could reasonably be expected to represent**

***reporting date*** **means the end of the financial year to which the financial report relates**

***reporting entity*** **means an entity (including an *economic entity*) in respect of which it is reasonable to expect the existence of users dependent on *general purpose financial reports* for information which will be useful to them for making and evaluating decisions about the allocation of scarce resources, and includes but is not limited to the following:**

**(a) a *listed corporation***

**(b) a *borrowing corporation***

**(c) a *company* which is not a subsidiary of a *holding company* incorporated in Australia and which is a subsidiary of a foreign company where that foreign company has its securities listed for quotation on a**

***stock market*** **or those securities are traded on a stock market**

***revenues*** **means inflows or other enhancements, or savings in outflows, of future economic benefits in the form of increases in assets or reductions in liabilities of the entity, other than those relating to contributions by owners, that result in an increase in equity during the financial year**

***stock market*** **is defined in the Corporations Law**

***subsidiary*** **means an entity which is controlled by a parent entity.**

## Acquisition costs

21.1.1 *Acquisition costs* relate to the costs incurred in acquiring specific life insurance policies during the financial year. They do not include the general growth and development costs incurred by a life insurer.

# CONFORMITY WITH INTERNATIONAL AND NEW ZEALAND ACCOUNTING STANDARDS

## Conformity with International Accounting Standards

As at the date of issuance of this Standard, the International Accounting Standards Committee has not issued a standard that corresponds with this Standard.

## Conformity with New Zealand Accounting Standards

This Standard is the result of a joint project between Australia and New Zealand. Except for differences arising from the different regulatory regimes, the Standards arising from the project have identical requirements.

## APPENDIX

# Sample Financial Reports

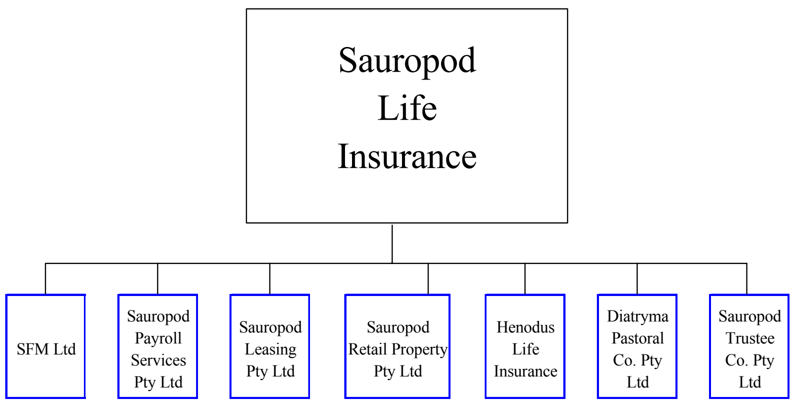
This Appendix forms part of the commentary and is provided for illustrative purposes only. The illustrative financial reports are not intended to be comprehensive and do not provide an example of all the information that is required to be reported by life insurers or parent entities. It should be noted that additional disclosures may be required by other Accounting Standards or under the *Life Insurance Act 1995*.

The group structure diagrams and associated explanations on pages 47 and 63 are not part of the illustrative financial reports.

## CONTENTS

# Sauropod Life Insurance

## Group Structure*




* All controlled entities are incorporated in Australia.
Sauropod Life Insurance has a 100% interest in all controlled entities except that it has a 60% interest in Sauropod Leasing Pty Ltd and a 55% interest in Diatryma Pastoral Co. Pty Ltd.
Sauropod Life Insurance is a wholly-owned subsidiary of Theropod Holdings.

## Sauropod Life Insurance

**Profit and Loss Statement**
**for the financial year ended 30 June 20X6**

| | | Company | | Consolidated | |
|---|---|---|---|---|---|
| | Note | **20X6 $m** | 20X5 $m | **20X6 $m** | 20X5 $m |
| Premium and related revenue | **4** | **255.0** | 219.0 | **270.0** | 229.0 |
| Outwards reinsurance expense | | **28.0** | 14.0 | **28.0** | 14.0 |
| | | **227.0** | 205.0 | **242.0** | 215.0 |
| Investment revenue | **5** | **910.0** | 850.0 | **940.0** | 875.0 |
| Other revenue | | **14.0** | 13.0 | **90.0** | 70.0 |
| Total net revenue | | **1,151.0** | 1,068.0 | **1,272.0** | 1,160.0 |
| Operating expenses | **6** | **1,024.0** | 995.0 | **1,132.0** | 1,089.0 |
| Operating profit before income tax | | **127.0** | 73.0 | **140.0** | 71.0 |
| Income tax expense | **7** | **40.3** | 35.0 | **50.8** | 34.0 |
| Operating profit after income tax | **8** | **86.7** | 38.0 | **89.2** | 37.0 |
| Outside equity interests in operating profit after income tax | | **-** | **-** | **5.0** | 1.0 |
| Operating profit after income tax and after outside equity interests | | **86.7** | 38.0 | **84.2** | 36.0 |
| Retained profits at the beginning of the financial year | | **146.0** | 117.0 | **138.0** | 111.0 |
| | | **232.7** | 155.0 | **222.2** | 147.0 |
| Dividends provided or paid | | **12.0** | 9.0 | **12.0** | 9.0 |
| Retained profits at the end of the financial year | **9** | **220.7** | 146.0 | **210.2** | 138.0 |

## Sauropod Life Insurance

**Balance Sheet**
**as at 30 June 20X6**

| | Note | Company | | Consolidated | |
|---|---|---|---|---|---|
| | | **20X6 $m** | 20X5 $m | **20X6 $m** | 20X5 $m |
| Cash | | **13.0** | 15.0 | **20.0** | 23.0 |
| Outstanding premiums | | **15.0** | 20.0 | **16.0** | 21.0 |
| Receivables | **10** | **102.0** | 109.0 | **149.0** | 115.0 |
| Equity security investments | **11** | **3,610.0** | 3,390.1 | **3,412.5** | 3,168.0 |
| Debt security investments | | **4,405.0** | 4,273.0 | **4,427.0** | 4,428.0 |
| Property investments | | **2,590.0** | 2,761.0 | **2,610.0** | 2,805.0 |
| Other investments | | **10.0** | 39.0 | **40.0** | 45.0 |
| Operating assets | | **25.0** | 30.0 | **175.0** | 145.0 |
| Excess of the net market values of interests in subsidiaries over their recognised net amounts | | **-** | - | **103.7** | 88.0 |
| Other assets | | **8.0** | - | **118.0** | 65.0 |
| **Total Assets** | | **10,778.0** | 10,637.1 | **11,071.2** | 10,903.0 |
| Creditors | | **137.3** | 139.0 | **148.5** | 146.0 |
| Provisions | **12** | **164.0** | 152.0 | **177.0** | 158.0 |
| Borrowings | **13** | **260.0** | 249.0 | **250.0** | 240.0 |
| Policy liabilities | **14** | **9,665.0** | 9,689.0 | **9,935.0** | 9,939.0 |
| Unvested policyholder benefits | | **291.0** | 231.1 | **295.0** | 234.0 |
| Other liabilities | | **25.0** | 21.0 | **30.0** | 30.0 |
| **Total Liabilities** | | **10,542.3** | 10,481.1 | **10,835.5** | 10,747.0 |
| **Net Assets** | | **235.7** | 156.0 | **235.7** | 156.0 |
| Share capital | | **15.0** | 10.0 | **15.0** | 10.0 |
| Retained profits | | **220.7** | 146.0 | **210.2** | 138.0 |
| | | **235.7** | 156.0 | **225.2** | 148.0 |
| Outside equity interests in subsidiaries | | **-** | - | **10.5** | 8.0 |
| **Total Equity** | | **235.7** | 156.0 | **235.7** | 156.0 |

# Sauropod Life Insurance

## Statement of Cash Flows
## for the financial year ended 30 June 20X6

| | Company | | Consolidated | |
|---|---|---|---|---|
| | **20X6 $m** | 20X5 $m | **20X6 $m** | 20X5 $m |
| **Cash Flows from Operating Activities** | | | | |
| Premiums received | **1,800.0** | 1,650.0 | **1,850.0** | 1,690.0 |
| Other revenue received (including sale of operating assets) | **31.0** | 21.0 | **59.5** | 60.5 |
| Payments to suppliers and employees | **(143.5)** | (159.0) | **(180.0)** | (195.0) |
| Policy payments | **(1,888.5)** | (1,668.0) | **(1,955.5)** | (1,720.5) |
| Fees and commissions paid | **(59.0)** | (57.0) | **(66.0)** | (62.0) |
| Interest paid | **(33.0)** | (14.0) | **(28.0)** | (48.0) |
| Income tax paid | **(42.0)** | (31.0) | **(87.5)** | (91.0) |
| Other payments (including purchase of operating assets) | **(11.5)** | (15.0) | **(38.0)** | (73.0) |
| Net Cash Used in Operating Activities | **(346.5)** | (273.0) | **(445.5)** | (439.0) |
| **Cash Flows from Investing Activities** | | | | |
| Dividends received | **135.5** | 112.0 | **143.5** | 118.0 |
| Interest received | **328.0** | 395.0 | **347.0** | 396.0 |
| Rentals received | **85.0** | 65.0 | **88.0** | 70.0 |
| Proceeds from sale of equity securities | **190.0** | 301.0 | **232.0** | 347.0 |
| Proceeds from sale of debt securities | **420.0** | 330.0 | **465.0** | 387.0 |
| Proceeds from sale of property investments | **633.0** | 110.0 | **660.0** | 181.0 |
| Purchase of equity securities | **(828.0)** | (203.0) | **(842.0)** | (211.0) |
| Purchase of debt securities | **(480.0)** | (404.0) | **(506.0)** | (414.0) |
| Purchase of freehold and leasehold property | **(156.0)** | (432.0) | **(159.0)** | (444.0) |
| Net Cash Provided by Investing Activities | **327.5** | 274.0 | **428.5** | 430.0 |
| **Cash Flows from Financing Activities** | | | | |
| Equity received from parent (Theropod Holdings) | **5.0** | - | **5.0** | - |
| Equity provided to controlled entities | **-** | (10.0) | **-** | - |
| Proceeds from borrowings | **31.0** | 3.0 | **34.0** | 3.0 |
| Repayment of borrowings | **(5.0)** | (1.0) | **(10.0)** | (5.0) |
| Dividends paid | **(12.0)** | (9.0) | **(13.0)** | (10.0) |
| Other payments | **(2.0)** | (1.0) | **(2.0)** | (1.0) |
| Net Cash Provided by (Used in) Financing Activities | **17.0** | (18.0) | **14.0** | (13.0) |
| Net increase (decrease) in cash held | **(2.0)** | (17.0) | **(3.0)** | (22.0) |
| Cash at the beginning of the period | **15.0** | 32.0 | **23.0** | 45.0 |
| Cash at the end of the period | **13.0** | 15.0 | **20.0** | 23.0 |

## Sauropod Life Insurance

**Notes to and forming part of the Financial Report**

**NOTE 1: ACCOUNTING POLICIES**

**Accounting Standards**

This financial report is a general purpose financial report prepared in accordance with applicable Accounting Standards and Urgent Issues Group Consensus Views.

**Premiums and claims**

Premiums and claims are separated into their revenue, expense and change in liability components. For unit-linked business, the components are identified progressively during the financial year. In relation to other policies, an actuarial model is used as at reporting date to determine a reliable measure of the revenue, expense and change in liability components.

**Liabilities**

Policy liabilities are measured at net present values of estimated future cash flows or, where the result would not be materially different, as the accumulated benefits available to policyholders. Other liabilities are measured at net present values and changes in their net present values arising from changes in the measurement of net present values are recognised in the profit and loss statement as revenues or expenses in the financial year in which the changes occur.

**Assets**

All assets are measured at net market values as at the reporting date and changes in their net market values arising from changes in the measurement of net market values are recognised in the profit and loss statement as revenues or expenses in the financial year in which the changes occur.

There is no active market for a large portion of the company's unlisted equity investments [20X6: $410m, 20X5: $320m]. Net market values have been determined for these investments based on discounted cash flow projections.

**NOTE 2: ACTUARIAL POLICIES AND METHODS**

The effective date of the actuarial report on policy liabilities and solvency reserves is 30 June 20X6. The actuarial report was prepared by [name] [qualifications] on [date]. The actuarial report indicates that [name] is satisfied as to the accuracy of the data upon which policy liabilities have been determined.

The amount of policy liabilities has been determined in accordance with methods and assumptions disclosed in this financial report and with the standards of the Life Insurance Actuarial Standards Board (LIASB).

**Disclosure of Assumptions**

Policy liabilities have been calculated in accordance with Actuarial Standard AS 1.01 "Valuation of Policy Liabilities" issued by the LIASB. The Actuarial Standard requires the policy liabilities to be calculated in a way which allows for the systematic release of planned margins as services are provided to policyholders and premiums are received.

The profit carriers used for the major product groups in order to achieve the systematic release of planned margins were as follows:

| **Major product groups** | **Profit carriers** |
|---|---|
| Investment-linked business (non-unitised) | Investment earnings or service charges |
| Investment account business | Interest credits |
| Traditional non-participating business, term insurance, group life and disability insurance | Claims or premiums |
| Traditional participating business | Bonuses |

Policy liabilities for unitised investment-linked business have been calculated using an accumulation method.

**(a) Discount rates**

The discount rates assumed are derived from the expected long-term average rates of return for the relevant asset pools based on a neutral asset mix for each pool. Discount rates assumed are:

| | |
|---|---|
| Australia – ordinary business (before tax basis) | 7.8%pa to 9.6%pa<br>(20X5: 7.6%pa to 9.6%pa) |
| Australia – superannuation business (after tax basis)<br>Complying<br><br>Non-complying | <br><br>6.8%pa to 8.5%pa<br>(20X5: 6.7%pa to 8.5%pa)<br>5.9%pa to 7.2%pa<br>(20X5: 6.7%pa to 8.5%pa) |
| New Zealand business (before tax basis) | 8.2%pa to 10.4%pa<br>(20X5: 8.2%pa to 10.4%pa) |

**(b) Inflation rates**

| | |
|---|---|
| Australia | 3.5%pa (20X5: 3.5%pa) |
| New Zealand | 2.0%pa (20X5: 2.0%pa) |

**(c) Future expenses and indexation**

Future maintenance expenses per policy have been assumed at current levels increased by the rate of inflation set out in (b) above.

Future investment expenses have been assumed to be at the same percentage of assets under management as currently applies.

Benefits and/or premiums under most of the regular premium policies are automatically indexed. Assumed future take-up of these indexation options has been based on the company's previous experience.

**(d) Rates of taxation**

Rates of taxation have been assumed in the future to remain at current levels. Refer to note 7 for details.

**(e) Mortality and morbidity**

For individually assessed business, future mortality was assumed in aggregate to be in the order of:

| | |
|---|---|
| Australia | 89% of IA85/90 (20X5: 89% of IA85/90) |
| New Zealand | 91% of IA85/90 (20X5: 91% of IA85/90) |

In applying this aggregate assumption to individual policies, adjustments were made for factors such as sex and product type.

For group life business, future mortality assumptions were based on the company's overall experience over recent years.

Future morbidity experience assumptions are based on US CIDA 85 tables, but with extensive adjustments to claim incidence and termination rates, having regard to industry experience in Australia.

**(f) Discontinuances**

Future rates of discontinuance for the major classes of business are assumed in aggregate to be in the order of:

| | |
|---|---|
| Investment-linked and investment account business<br>– single premium<br>– regular premium | <br><br>17.5%pa (20X5: 17.5%pa)<br>15%pa (20X5: 15%pa) |
| Term life insurance | 15%pa (20X5: 15%pa) |
| Disability income insurance | 19%pa (20X5: 19%pa) |
| Endowment insurance | 16%pa (20X5: 15%pa) |
| Whole of life insurance | 11%pa (20X5: 11%pa) |

Assumed rates may vary by sub-grouping within a class and vary according to the length of time tranches of business have been in force.

**(g) Surrender values**

Surrender values are based on the provisions specified in policy contracts and include a recovery of policy establishment and maintenance costs.

**(h) Unit prices**

An accumulation approach has been used to determine policy liabilities for unit-linked business and no assumptions are needed about rates of growth of unit prices.

**(i) Future participating benefits**

For participating business, the company's policy is to set bonus rates such that over long periods, the returns to policyholders are commensurate with the investment returns achieved on relevant assets, together with other sources of profit arising from this business. Distributions are split between policyholders and shareholders with the valuation allowing for shareholders to share in distributions at the maximum allowable rate of 20%. In applying the policyholders' share of distributions to provide bonuses, consideration is given to equity between generations of policyholders and equity between the various classes and sizes of policies in force. Assumed future bonus rates included in policy liabilities were set such that the present value of policy liabilities equates to the present value of the assets supporting the business together with assumed future investment returns, allowing for the shareholders' right to participate in distributions.

Assumed future bonus rates for the major classes of individual participating business were:

| | |
|---|---|
| Endowment insurance policies<br>*bonus rate on sum assured<br>*bonus rate on existing bonuses | <br>1.855%pa (20X5: 1.821%pa)<br>2.266%pa (20X5: 2.193%pa) |
| Whole of life policies<br>*bonus rate on sum assured<br>*bonus rate on existing bonuses | <br>1.984%pa (20X5: 1.964%pa)<br>2.476%pa (20X5: 2.471%pa) |

These rates are in addition to contractual returns on participating policies.

## NOTE 3: DISCLOSURES ON ASSET RESTRICTIONS, MANAGED ASSETS AND TRUSTEE ACTIVITIES

### (a) Restrictions on assets

Investments held in the Life Funds can only be used within the restrictions imposed under the *Life Insurance Act 1995*. The main restrictions are that the assets in a Fund can only be used to meet the liabilities and expenses of that Fund, to acquire investments to further the business of the Fund or as distributions when solvency and capital adequacy requirements are met. Participating policyholders can receive a distribution when solvency requirements are met, whilst shareholders can only receive a distribution when the higher level of capital adequacy requirements are met.

### (b) Managed assets

Sauropod Life Insurance controls SFM Ltd which manages two unit trusts with a combined total of $500 million of assets under management. Arrangements are in place to ensure that the asset management activities of SFM are managed separately from Sauropod Life Insurance.

**(c) Trustee activities**

Sauropod Trustee Co. Pty Ltd acts as trustee in relation to superannuation policies issued by Sauropod Life Insurance. Arrangements are in place to ensure that the activities of Sauropod Trustee Co. Pty Ltd are managed separately.

| | Company | | Consolidated | |
|---|---|---|---|---|
| | **20X6** | 20X5 | **20X6** | 20X5 |
| | **$m** | $m | **$m** | $m |
| **NOTE 4: PREMIUM AND RELATED REVENUE** | | | | |
| Premium revenue | **247.5** | 213.5 | **262.5** | 223.5 |
| Inwards reinsurance premiums | **5.0** | 4.0 | **5.0** | 4.0 |
| Reinsurance recoveries | **2.5** | 1.5 | **2.5** | 1.5 |
| Total premium and related revenue | **255.0** | 219.0 | **270.0** | 229.0 |
| Total premiums received or receivable | **1,815.0** | 1,670.0 | **1,866.0** | 1,711.0 |

**NOTE 5: INVESTMENT REVENUE**

Including realised and unrealised gains and losses

| | | | | |
|---|---|---|---|---|
| Equity securities | **323.0** | 276.0 | **336.0** | 314.5 |
| Debt securities | **347.0** | 371.5 | **352.5** | 350.0 |
| Property | **225.0** | 195.0 | **230.0** | 195.0 |
| Other | **15.0** | 7.5 | **21.5** | 15.5 |
| Total investment revenue | **910.0** | 850.0 | **940.0** | 875.0 |

| | Company | | Consolidated | |
|---|---|---|---|---|
| | **20X6** | 20X5 | **20X6** | 20X5 |
| | **$m** | $m | **$m** | $m |
| **NOTE 6: OPERATING EXPENSES** | | | | |
| Acquisition | **60.0** | 62.0 | **61.5** | 67.0 |
| Policy maintenance | **123.0** | 149.5 | **127.5** | 153.8 |
| Investment management | **29.0** | 35.0 | **30.0** | 37.0 |
| Interest [including any gain or loss on borrowings] | **10.0** | (8.0) | **10.0** | (8.0) |
| Claims expense | **807.0** | 730.0 | **847.8** | 747.6 |
| Other changes in policy liabilities * | **(6.0)** | 25.0 | **(5.8)** | 27.6 |
| Other | **1.0** | 1.5 | **61.0** | 64.0 |
| Total operating expenses | **1,024.0** | 995.0 | **1,132.0** | 1,089.0 |
| Total claims paid or payable | **1,890.0** | 1,670.0 | **1,975.0** | 1,735.0 |

* Increases in policy liabilities includes the change in unvested policyholder benefits and bonuses vested in policyholders during the financial year.

## NOTE 7: INCOME TAX EXPENSE

The income tax expense of Sauropod Life Insurance is partly determined on a product-basis and partly determined on a profit-basis. The income tax expense of Sauropod Life Insurance has been determined after aggregating various classes of business, each with different tax rates. The rates of taxation applicable to the taxable income of significant classes of business are as follows:

| Class of Business | **20X6** | 20X5 |
|---|---|---|
| Ordinary life insurance business | **39%** | 39% |
| Complying superannuation | **15%** | 15% |
| Controlled companies | **36%** | 36% |
| Current pension business | **Exempt** | Exempt |
| Non-complying superannuation | **47%** | 47% |
| Immediate annuity business | **Exempt** | Exempt |
| New Zealand business | **33%** | 33% |
| RSA business | **15%** | 15% |
| Other business (including accident and disability) | **39%** | 39% |
| Shareholder (general) funds | **36%** | 36% |

**Taxation basis**

The principal elements for the calculation of the taxable income for each class of business are as follows:

*Assessable income*

1. Complying superannuation business - taxable contributions transferred from superannuation funds, specified rollover amounts and investment income

2. Non-complying superannuation business - investment income

3. Other business - accident and disability premiums earned and investment income

4. Shareholder (general) funds and ordinary life insurance business - investment income

5. RSA business – taxable contributions and investment income credited to policyholders.

The gains and losses on sale of investments to the extent referable to the complying superannuation business are determined under the capital gains tax provisions of the *Income Tax Assessment Act* (ITAA). The exceptions are gains on fixed interest securities and foreign exchange gains or losses referable to the superannuation business which are taxed primarily under the ordinary income provisions.

The gains and losses on the sale of investments to the extent referable to other taxable classes of business are taxed primarily under the ordinary income provisions, with the capital gains tax provisions potentially applying depending on the circumstance.

*Allowable deductions*

The allowable deductions for each taxable class of business in Australia include:

1. acquisition costs (such as commissions) in relation to investment related life insurance business, superannuation business and “other business”

2. other expenses referable to the business (such as investment expenses)

3. an allocation of the general management expenses of the company.

These deductions are then allocated to each class of business in accordance with the basis specified in the ITAA (which may or may not reflect the allocation of the expense for accounting purposes).

Allowable deductions in respect of "other business" within the Life Funds also include accident and disability claims and the movement during the period in the policy liability in respect of that business (which may differ from the policy liability recognised for accounting purposes).

| | Company | | Consolidated | |
|---|---|---|---|---|
| | **20X6** | 20X5 | **20X6** | 20X5 |
| | **$m** | $m | **$m** | $m |

**NOTE 8: OPERATING PROFIT AFTER INCOME TAX**

| | | | | |
|---|---|---|---|---|
| Operating profit after income tax arose from | | | | |
| Movements in policy liabilities: | | | | |
| Planned margins of revenues over expenses released | **123.5** | 124.1 | **129.8** | 126.1 |
| Difference between actual and assumed experience | **22.4** | (23.0) | **21.9** | (24.7) |
| Other | **(73.3)** | (66.7) | **(86.7)** | (69.3) |
| Investment earnings on assets in excess of policy liabilities | **14.1** | 3.6 | **19.3** | 4.7 |
| Other | **-** | - | **4.9** | 0.2 |
| Operating profit after income tax | **86.7** | 38.0 | **89.2** | 37.0 |

Paragraph 15.5 requires that the disclosures in Note 8 are separated between policyholder and shareholder interests.

**NOTE 9: RECONCILIATION OF CORPORATIONS LAW RESULTS WITH LIFE INSURANCE ACT RESULTS**

| | | | | |
|---|---|---|---|---|
| Operating profit after income tax | **86.7** | 38.0 | **89.2** | 37.0 |
| Plus: participating benefits expense (at cost of bonus) | **73.3** | 66.7 | **86.7** | 69.3 |
| Plus: changes in unvested policyholder benefits liability | **59.9** | 55.0 | **61.0** | 56.0 |
| Life Insurance Act profit after tax | **219.9** | 159.7 | **236.9** | 162.3 |
| Retained profits | **220.7** | 146.0 | **210.2** | 138.0 |
| Plus: unvested policyholder benefits liability | **291.0** | 231.1 | **295.0** | 234.0 |
| Life Insurance Act retained profits | **511.7** | 377.1 | **505.2** | 372.0 |

| | Company | | Consolidated | |
|---|---|---|---|---|
| | **20X6** | 20X5 | **20X6** | 20X5 |
| | **$m** | $m | **$m** | $m |

## NOTE 10: RECEIVABLES

| | | | | |
|---|---|---|---|---|
| Reinsurance recoveries receivable | **3.0** | 2.0 | **3.0** | 2.0 |
| Other receivables | **99.0** | 107.0 | **146.0** | 113.0 |
| Total receivables | **102.0** | 109.0 | **149.0** | 115.0 |

## NOTE 11: EQUITY SECURITY INVESTMENTS

| | | | | |
|---|---|---|---|---|
| Ordinary | **3,241.0** | 3,058.1 | **3,412.5** | 3,168.0 |
| Controlled entities | **369.0** | 332.0 | **-** | - |
| Total equity security investments | **3,610.0** | 3,390.1 | **3,412.5** | 3,168.0 |

## NOTE 12: PROVISIONS

| | | | | |
|---|---|---|---|---|
| Income tax | **67.0** | 62.0 | **75.0** | 73.0 |
| Employee entitlements | **50.0** | 45.0 | **53.0** | 52.0 |
| Other provisions | **47.0** | 45.0 | **49.0** | 33.0 |
| Total provisions | **164.0** | 152.0 | **177.0** | 158.0 |

## NOTE 13: BORROWINGS

| | | | | |
|---|---|---|---|---|
| Subordinated debt | **200.0** | 230.0 | **200.0** | 230.0 |
| Loans from controlled entities | **15.0** | 16.0 | **-** | - |
| Other borrowings | **45.0** | 3.0 | **50.0** | 10.0 |
| Total borrowings | **260.0** | 249.0 | **250.0** | 240.0 |

## NOTE 14: POLICY LIABILITIES

| | | | | |
|---|---|---|---|---|
| Future policy benefits * | **10,261.0** | 10,340.0 | **10,531.0** | 10,590.0 |
| Future bonuses | **1,500.0** | 1,400.0 | **1,500.0** | 1,400.0 |
| Future expenses | **630.0** | 660.0 | **630.0** | 660.0 |
| Future profit margins | **176.0** | 157.0 | **176.0** | 157.0 |
| Future charges for acquisition expenses | **(76.0)** | (70.0) | **(76.0)** | (70.0) |
| Balance of future premiums | **(2,826.0)** | (2,798.0) | **(2,826.0)** | (2,798.0) |
| Total policy liabilities | **9,665.0** | 9,689.0 | **9,935.0** | 9,939.0 |
| Policy liabilities subject to capital guarantees | **922.0** | 1,011.0 | **922.0** | 1,011.0 |

*Future policy benefits include bonuses vested in policyholders in current and prior periods.

| NOTE 15: DISAGGREGATED INFORMATION BY FUND | Company | | | | | |
|---|---|---|---|---|---|---|
| | Australian investment-linked | NZ investment-linked | Total investment-linked | Australian non-investment linked | General share-holders | Total Funds |
| **20X6** | **$m** | **$m** | **$m** | **$m** | **$m** | **$m** |
| Investment assets | **6,080.0** | **1,089.0** | **7,169.0** | **3,334.0** | **112.0** | **10,615.0** |
| Other assets | **83.0** | **15.0** | **98.0** | **55.0** | **10.0** | **163.0** |
| Policy liabilities | **5,558.0** | **1,020.0** | **6,578.0** | **3,087.0** | **-** | **9,665.0** |
| Unvested policyholder benefits | **-** | **-** | **-** | **291.0** | **-** | **291.0** |
| Other liabilities | **296.3** | **44.0** | **340.3** | **241.9** | **4.1** | **586.3** |
| Retained profits | **34.0** | **22.0** | **56.0** | **142.7** | **22.0** | **220.7** |
| Premium revenue | **42.0** | **4.0** | **46.0** | **209.0** | **-** | **255.0** |
| Investment revenue | **560.7** | **100.0** | **660.7** | **241.0** | **8.3** | **910.0** |
| Claims expense | **440.0** | **90.0** | **530.0** | **275.0** | **2.0** | **807.0** |
| Other operating expenses | **119.0** | **22.0** | **141.0** | **75.1** | **0.9** | **217.0** |
| Operating profit (loss) before tax | **43.7** | **(8.0)** | **35.7** | **85.9** | **5.4** | **127.0** |
| Operating profit (loss) after tax | **23.0** | **(3.0)** | **20.0** | **63.5** | **3.2** | **86.7** |
| Transfer from general fund | **5.0** | **-** | **5.0** | **-** | **(5.0)** | **-** |

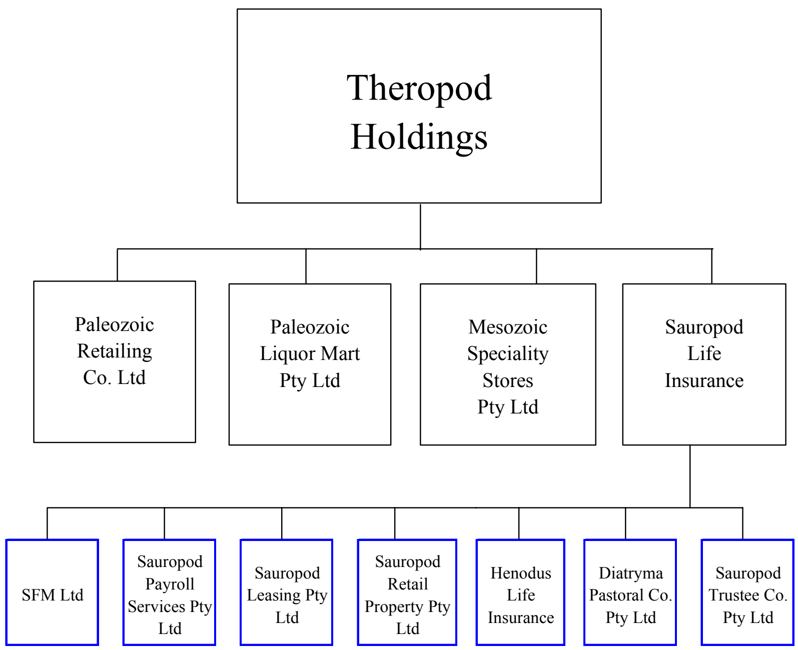
This information should also be presented for the economic entity of which Sauropod is the parent entity

**NOTE 15: DISAGGREGATED INFORMATION BY FUND continued**

| | Company | | | | | |
|---|---|---|---|---|---|---|
| | Australian investment-linked | NZ investment-linked | Total investment-linked | Australian non-investment linked | General share-holders | Total Funds |
| **20X5** | **$m** | **$m** | **$m** | **$m** | **$m** | **$m** |
| Investment assets | 6,100.0 | 1,221.0 | 7,321.0 | 3,036.0 | 106.1 | 10,463.1 |
| Other assets | 90.0 | 12.0 | 102.0 | 60.0 | 12.0 | 174.0 |
| Policy liabilities | 5,608.0 | 998.0 | 6,606.0 | 3,083.0 | - | 9,689.0 |
| Unvested policyholder benefits | - | - | - | 231.1 | - | 231.1 |
| Other liabilities | 285.0 | 36.0 | 321.0 | 235.0 | 5.0 | 561.0 |
| Retained profits | 11.0 | 25.0 | 36.0 | 91.3 | 18.7 | 146.0 |
| Premium revenue | 46.0 | 5.5 | 51.5 | 167.5 | - | 219.0 |
| Investment revenue | 488.0 | 95.0 | 583.0 | 240.4 | 26.6 | 850.0 |
| Claims expense | 375.0 | 75.0 | 450.0 | 265.0 | 15.0 | 730.0 |
| Other operating expenses | 135.0 | 29.6 | 164.6 | 95.4 | 5.0 | 265.0 |
| Operating profit before tax | 24.0 | 0.9 | 24.9 | 41.5 | 6.6 | 73.0 |
| Operating profit after tax | 8.6 | 0.4 | 9.0 | 25.0 | 4.0 | 38.0 |
| Transfer from general fund | - | - | - | - | - | - |

# Theropod Holdings

## Group Structure*




* All controlled entities are incorporated in Australia.
Theropod Holdings has a 100% interest in all controlled entities except that it has a 75% interest in Mesozoic Speciality Stores Pty Ltd, a 60% interest in Sauropod Leasing Pty Ltd and a 55% interest in Diatryma Pastoral Co. Pty Ltd.

*Information similar to that in the Sauropod Life Insurance financial report notes 1 to 15 would be included in, or presented with, the Theropod Holdings financial report, where the information is material in the context of the economic entity. For the sake of brevity, such information has not been included in the Theropod Holdings financial report.*

## Theropod Holdings

### Profit and Loss Statement
### for the financial year ended 30 June 20X6

| | Note | Company | | Consolidated | |
|---|---|---|---|---|---|
| | | **20X6** | 20X5 | **20X6** | 20X5 |
| | | **$m** | $m | **$m** | $m |
| Operating revenue | **2** | **1,042.3** | 931.3 | **5,708.7** | 5,164.2 |
| Operating profit before income tax | | **86.3** | 119.2 | **230.5** | 297.3 |
| Income tax expense | | **22.8** | 25.5 | **80.3** | 94.1 |
| Operating profit after income tax | | **63.5** | 93.7 | **150.2** | 203.2 |
| Outside equity interests in operating profit after income tax | | **-** | - | **13.7** | 20.1 |
| Operating profit after income tax and outside equity interests | | **63.5** | 93.7 | **136.5** | 183.1 |
| Retained profits at the beginning of the financial year | | **109.4** | 127.9 | **585.6** | 514.7 |
| | | **172.9** | 221.6 | **722.1** | 697.8 |
| Dividends paid or provided | | **45.7** | 112.2 | **45.7** | 112.2 |
| Retained profits at the end of the financial year | | **127.2** | 109.4 | **676.4** | 585.6 |

# Theropod Holdings

## Balance Sheet
## as at 30 June 20X6

| | Note | Company | | Consolidated | |
|---|---|---|---|---|---|
| | | **20X6** | 20X5 | **20X6** | 20X5 |
| | | **$m** | $m | **$m** | $m |
| **Current Assets** | | | | | |
| Cash | | **20.1** | 1.2 | **48.2** | 33.1 |
| Receivables | | **10.0** | 7.4 | **407.4** | 287.3 |
| Inventories | | **26.5** | 23.2 | **603.1** | 560.8 |
| Other current assets | | **12.6** | 10.8 | **23.6** | 21.2 |
| Total Current Assets | | **69.2** | 42.6 | **1,082.3** | 902.4 |
| **Non-Current Assets** | | | | | |
| Investments at cost | **3** | **377.3** | 372.6 | **4.9** | 5.1 |
| Operating assets | | **73.5** | 42.6 | **593.5** | 548.3 |
| Intangibles | | **7.4** | 4.9 | **11.9** | 9.4 |
| Other non-current assets | | **18.3** | 8.4 | **43.8** | 41.1 |
| Total Non-Current Assets | | **476.5** | 428.5 | **654.1** | 603.9 |
| Investments relating to Life Insurance Business | | **-** | - | **10,410.0** | 10,420.0 |
| Excess of the Net Market Values of the Interests of Sauropod Life Insurance in its Subsidiaries over their Recognised Net Amounts | | **-** | - | **103.7** | 88.0 |
| **Total Assets** | | **545.7** | 471.1 | **12,250.1** | 12,014.3 |
| **Current Liabilities** | | | | | |
| Creditors and borrowings | | **48.4** | 39.9 | **433.4** | 405.5 |
| Provisions | | **47.2** | 52.6 | **163.0** | 184.9 |
| Total Current Liabilities | | **95.6** | 92.5 | **596.4** | 590.4 |
| **Non-Current Liabilities** | | | | | |
| Creditors and borrowings | | **79.4** | 55.1 | **295.7** | 260.9 |
| Provisions | | **65.1** | 63.3 | **154.7** | 139.5 |
| Other non-current liabilities | | **40.0** | 40.0 | **45.0** | 48.0 |
| Total Non-Current Liabilities | | **184.5** | 158.4 | **495.4** | 448.4 |
| Life Insurance Policy Liabilities | | **-** | - | **9,935.0** | 9,939.0 |
| Unvested policyholder benefits | | **-** | - | **295.0** | 234.0 |
| **Total Liabilities** | | **280.1** | 250.9 | **11,321.8** | 11,211.8 |
| **Net Assets** | | **265.6** | 220.2 | **928.3** | 802.5 |
| **Equity** | | | | | |
| Share capital | | **95.9** | 93.6 | **95.9** | 93.6 |
| Reserves | | **42.5** | 17.2 | **90.0** | 64.8 |
| Retained profits | | **127.2** | 109.4 | **676.4** | 585.6 |
| Outside equity interests in subsidiaries | | **-** | - | **66.0** | 58.5 |
| **Total Equity** | | **265.6** | 220.2 | **928.3** | 802.5 |

# Theropod Holdings

**Statement of Cash Flows**
**for the financial year ended 30 June 20X6**

| | Company | | Consolidated | |
|---|---|---|---|---|
| | **20X6** | 20X5 | **20X6** | 20X5 |
| | **$m** | $m | **$m** | $m |
| **Cash Flows from Operating Activities** | | | | |
| Receipts from retail customers | **1,403.4** | 1,297.5 | **4,292.4** | 3,923.3 |
| Receipts from tenants | **8.0** | 16.6 | **155.8** | 119.9 |
| Premiums received | **-** | - | **1,850.0** | 1,690.0 |
| Dividends from related entities | **56.4** | 57.1 | **-** | - |
| Dividends – other | **-** | - | **143.5** | 118.0 |
| Interest received | **0.8** | 0.1 | **350.9** | 398.4 |
| Payments to suppliers and employees | **(1,390.8)** | (1,253.1) | **(3,884.2)** | (3,907.6) |
| Interest paid | **(10.1)** | (2.4) | **(98.2)** | (79.8) |
| Income tax paid | **(12.4)** | (6.5) | **(158.7)** | (119.5) |
| Fees and commissions paid | **-** | - | **(66.0)** | (62.0) |
| Policy payments | **-** | - | **(1,955.5)** | (1,720.5) |
| Net Cash Provided by Operating Activities | **55.3** | 109.3 | **630.0** | 360.2 |
| **Cash Flows from Investing Activities** | | | | |
| Purchases of property and equipment | **(11.6)** | (18.7) | **(42.5)** | (507.5) |
| Proceeds from sale of property and equipment | **0.5** | 14.4 | **60.6** | 23.6 |
| Additional equity for life insurance business | **(5.0)** | - | **-** | - |
| Purchase of equity securities | **-** | - | **(842.0)** | (211.0) |
| Sale of equity securities | **-** | - | **232.2** | 420.1 |
| Net Cash Flows Used in Investing Activities | **(16.1)** | (4.3) | **(591.7)** | (274.8) |
| **Cash Flows from Financing Activities** | | | | |
| Deposits made | **(0.9)** | - | **(1.5)** | (1.0) |
| Proceeds from borrowings | **25.7** | 5.5 | **101.4** | 55.5 |
| Repayment of borrowings | **-** | (20.0) | **(73.0)** | (81.9) |
| Dividends paid | **(45.1)** | (89.8) | **(48.1)** | (92.8) |
| Other payments | **-** | - | **(2.0)** | (1.0) |
| Net Cash Used in Financing Activities | **(20.3)** | (104.3) | **(23.2)** | (121.2) |
| Net increase (decrease) in cash held | **18.9** | 0.7 | **15.1** | (35.8) |
| Cash at the beginning of the period | **1.2** | 0.5 | **33.1** | 68.9 |
| Cash at the end of the period | **20.1** | 1.2 | **48.2** | 33.1 |

# Theropod Holdings

**Notes to and forming part of the financial report**

**NOTE 1: ACCOUNTING POLICIES**

**Accounting standards**

This financial report is a general purpose financial report prepared in accordance with applicable Accounting Standards and Urgent Issues Group Consensus Views.

**Measurement and classification**

In relation to the group's retailing business, assets, liabilities, revenues and expenses are measured on the basis of historical costs and modified historical costs. Employee entitlements are measured at their present values.

In relation to the group's life insurance business, which is conducted by Sauropod Life Insurance and its subsidiary Henodus Life Insurance, assets, liabilities, revenues and expenses are measured on the basis of net market values and net present values.

In the group's consolidated balance sheet, the following are separately identified:

(a) investment assets relating to the life insurance business, measured at net market values;

(b) excess of the net market values of the interests of Sauropod Life Insurance in its subsidiaries over their recognised net amounts; and

(c) life insurance policy liabilities and unvested policyholder benefits, measured at net present value.

Other categories of assets and liabilities of the group are an aggregation of retail and life insurance assets and liabilities.

Consolidated operating assets include retail operating assets measured at historical costs and revalued amounts (both depreciated) and life insurance operating assets measured at net market values.

Consolidated current creditors and borrowings include all of Sauropod Life Insurance's creditors and some of its borrowings. Consolidated non-current creditors and borrowings include the balance of Sauropod Life Insurance's borrowings and all of its "other liabilities". The non-current borrowings and "other liabilities" relating to life insurance operations are measured at net present values, and changes to those net present values, as well as borrowing costs, are recognised as expenses (and, in some cases, revenues) of the period. The borrowings and other liabilities relating to the retail operations are measured at their face values with only borrowing costs recognised as expenses of the period.

**Life insurance subsidiary**

The company's investment in Sauropod Life Insurance is measured at cost.

| | Company | | Consolidated | |
|---|---|---|---|---|
| | **20X6 $m** | 20X5 $m | **20X6 $m** | 20X5 $m |
| **NOTE 2: OPERATING REVENUE** | | | | |
| Retail sales revenue | **903.8** | 783.7 | **4,294.9** | 3,909.3 |
| Discounts and other revenue | **18.8** | 17.0 | **140.9** | 125.4 |
| Investment revenue | **0.8** | 0.1 | **942.9** | 878.4 |
| Sale of property, plant and equipment | **0.5** | 14.4 | **60.0** | 22.1 |
| Dividends received from controlled entities | **118.4** | 116.1 | **-** | - |
| Premium and related revenue | **-** | - | **270.0** | 229.0 |
| Total operating revenue | **1,042.3** | 931.3 | **5,708.7** | 5,164.2 |
| **NOTE 3: INVESTMENTS AT COST** | | | | |
| Shares in controlled entities | **361.7** | 356.7 | **-** | - |
| Loans to controlled entities | **13.9** | 13.9 | **-** | - |
| Other | **1.7** | 2.0 | **4.9** | 5.1 |
| Total investments at cost | **377.3** | 372.6 | **4.9** | 5.1 |

| NOTE 4: INDUSTRY SEGMENT INFORMATION | Retailing | | Life Insurance* | | Other | | Eliminations | | Consolidated | |
|---|---|---|---|---|---|---|---|---|---|---|
| | **20X6** **$m** | 20X5 $m | **20X6** **$m** | 20X5 $m | **20X6** **$m** | 20X5 $m | **20X6** **$m** | 20X5 $m | **20X6** **$m** | 20X5 $m |
| Segment revenue | | | | | | | | | | |
| From customers outside the group | **4,408.7** | 3,990.2 | **1,224.0** | 1,117.0 | **76.0** | 57.0 | **-** | - | **5,708.7** | 5,164.2 |
| Intersegment | **-** | - | **9.0** | 8.0 | **12.0** | 10.0 | **(21.0)** | (18.0) | **-** | - |
| Operating revenue | **4,408.7** | 3,990.2 | **1,233.0** | 1,125.0 | **88.0** | 67.0 | **(21.0)** | (18.0) | **5,708.7** | 5,164.2 |
| Segment result | **108.9** | 234.3 | **153.0** | 92.0 | **8.6** | 9.0 | **(0.6)** | (0.4) | **269.9** | 334.9 |
| Unallocated expenses | | | | | | | | | **(39.4)** | (37.6) |
| Operating profit before income tax | | | | | | | | | **230.5** | 297.3 |
| Income tax expense | | | | | | | | | **(80.3)** | (94.1) |
| Operating profit after income tax | | | | | | | | | **150.2** | 203.2 |
| Segment assets | **978.9** | 897.6 | **10,935.4** | 10,833.1 | **285.3** | 251.9 | **-** | - | **12,199.6** | 11,982.6 |
| Unallocated assets | | | | | | | | | **50.5** | 31.7 |
| Total assets | | | | | | | | | **12,250.1** | 12,014.3 |

The group has retail operations in Australia and life insurance operations in Australia and New Zealand. In the context of the group, the New Zealand life insurance operations are not a material geographical segment.

*The life insurance segment includes Sauropod Life Insurance and its subsidiary Henodus Life Insurance.

# DEVELOPMENT OF THE STANDARD

This section does not form part of the Standard. The Standard was developed as a joint project by the Australian Accounting Standards Board and the New Zealand Financial Reporting Standards Board (the Boards). This section summarises the development of the Standard and the Boards' consideration of the key issues dealt with in the Standard.

1 The issue of the Standard follows consideration of the responses received on Proposed Accounting Standard ED 73/ED-79 "Financial Reporting of Life Insurance Business", which was prepared by the Boards and released in July 1996.

## Principal Features of ED 73/ED-79 Retained in the Standard

2 The Standard retains the basic structure and content of ED 73/ ED-79. Assets are required to be recognised at net market values and liabilities are required to be recognised at net present values. Premiums and claims are required to be separated into their revenue, expense and change in liability components, except where this is not practicable.

## Noteworthy Differences from ED 73/ED-79

3 ED 73/ED-79 excluded life insurers that had been created for purposes other than writing life insurance business from the definition of a life insurer. The Standard applies to all life insurers.

4 ED 73/ED-79 proposed that policyholder retained profits be recognised as equity. The Standard requires that policyholder "retained profits" are classified as liabilities where they must be paid to participating policyholders, even if the timing and identification of the recipient policyholders is at the discretion of the life insurer.

5 ED 73/ED-79 was silent with respect to the treatment of a deficiency of the net market value of a life insurer's interest in a subsidiary over the net amount of that subsidiary's assets and liabilities. The Standard requires that a net deficiency is recognised as a revenue.

## Future Developments

6 ED 73/ED-79 was silent with respect to the treatment of the acquisition of a block of life insurance policies. The Boards intend to develop requirements for the recognition and measurement of a

block of life insurance policies acquired by a life insurer as a separate project.