

AASB Exposure Draft

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Amendments to AASB 1038 arising from AASB 10 in relation to consolidation and interests of policyholders

Comments to the AASB by 7 August 2013



Australian Government

**Australian Accounting
Standards Board**

Commenting on this AASB Exposure Draft

Comments on this Exposure Draft are requested by 7 August 2013.
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All submissions on possible, proposed or existing financial reporting requirements, or on the standard-setting process, will be placed on the public record unless the Chairman of the AASB agrees to submissions being treated as confidential. The latter will occur only if the public interest warrants such treatment.

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This Exposure Draft is available on the AASB website: www.aasb.gov.au.
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AASB 2013-XX AMENDMENTS TO AASB 1038 ARISING FROM
AASB 10 IN RELATION TO CONSOLIDATION AND INTERESTS OF
POLICYHOLDERS**

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[Draft] Australian Accounting Standard AASB 2013-XX <i>Amendments to AASB 1038 arising from AASB 10 in relation to consolidation and interests of policyholders</i> is set out in paragraphs 1 – 8.

PREFACE

Introduction

Australian Accounting Standards

The Australian Accounting Standards Board (AASB) makes Australian Accounting Standards, including Interpretations, to be applied by:

- (a) entities required by the *Corporations Act 2001* to prepare financial reports;
- (b) governments in preparing financial statements for the whole of government and the General Government Sector (GGS); and
- (c) entities in the private or public for-profit or not-for-profit sectors that are reporting entities or that prepare general purpose financial statements.

AASB 1053 *Application of Tiers of Australian Accounting Standards* establishes a differential reporting framework consisting of two tiers of reporting requirements for preparing general purpose financial statements:

- (a) Tier 1: Australian Accounting Standards; and
- (b) Tier 2: Australian Accounting Standards – Reduced Disclosure Requirements.

Tier 1 requirements incorporate International Financial Reporting Standards (IFRSs), including Interpretations, issued by the International Accounting Standards Board (IASB), with the addition of paragraphs on the applicability of each Standard in the Australian environment.

Publicly accountable for-profit private sector entities are required to adopt Tier 1 requirements, and therefore are required to comply with IFRSs. Furthermore, other for-profit private sector entities complying with Tier 1 requirements will simultaneously comply with IFRSs. Some other entities complying with Tier 1 requirements will also simultaneously comply with IFRSs.

Tier 2 requirements comprise the recognition, measurement and presentation requirements of Tier 1 but substantially reduced disclosure requirements in comparison with Tier 1.

Australian Accounting Standards also include requirements that are specific to Australian entities. These requirements may be located in Australian

Accounting Standards that incorporate IFRSs or in other Australian Accounting Standards. In most instances, these requirements are either restricted to the not-for-profit or public sectors or include additional disclosures that address domestic, regulatory or other issues. These requirements do not prevent publicly accountable for-profit private sector entities from complying with IFRSs. In developing requirements for public sector entities, the AASB considers the requirements of International Public Sector Accounting Standards (IPSASs), as issued by the International Public Sector Accounting Standards Board (IPSASB) of the International Federation of Accountants.

Exposure Drafts

The publication of an Exposure Draft is part of the due process that the AASB follows before making a new Australian Accounting Standard or amending an existing one. Exposure Drafts are designed to seek public comment on the AASB's proposals for new Australian Accounting Standards or amendments to existing Standards.

Reason for Issuing this Exposure Draft

In August 2011, the AASB made AASB 10 *Consolidated Financial Statements* (which incorporates IFRS 10 *Consolidated Financial Statements*). Although the consolidation requirements in AASB 10 and its predecessor AASB 127 *Consolidated and Separate Financial Statements* (which superseded AASB 1024 *Consolidated Accounts*, upon which the consolidation requirements in AASB 1038 *Life Insurance Contracts* were originally based) are both based on the concept of 'control', AASB 10 contains a revised definition of control and specific requirements in relation to control of specified assets in deemed separate entities.

The reason for issuing this Exposure Draft is to seek comments on the proposal to remove the consolidation requirements from AASB 1038, including the explicit requirement for a life insurer to consolidate policyholders' interests, and thereby leave AASB 10 as the sole source of consolidation requirements applicable to life insurer entities.

Main Features of this Exposure Draft

As noted immediately above, this Exposure Draft proposes to remove the specific requirements in relation to consolidation from AASB 1038 (in particular, paragraphs 1.1.1, 4.1, 4.1.1, and 4.2 – 4.2.2), which would leave AASB 10 as the sole source for consolidation requirements applicable to life insurer entities.

In its October 2011 meeting the AASB decided there is no need to create Tier 2 general purpose financial reporting requirements in respect of accounting for insurance contracts, based on the Board's view that entities with material insurance contracts that prepare general purpose financial statements would all have public accountability and therefore need to apply Tier 1 requirements. The proposals in this Exposure Draft therefore have no Tier 2 implications.

Application Date

It is proposed that this Standard be applicable to annual reporting periods beginning on or after 1 January 2014 with early adoption permitted for annual reporting periods beginning on or after 1 January 2005.

Request for Comments

Comments are invited on any of the proposals in this Exposure Draft by 7 August 2013. Submissions play an important role in the decisions that the AASB will make in regard to a Standard. The AASB would prefer that respondents express a clear overall opinion on whether the proposals, as a whole, are supported and that this opinion be supplemented by detailed comments, whether supportive or critical, on the major issues. The AASB regards supportive and critical comments as essential to a balanced review of the issues and will consider all submissions, whether they address all specific matters, additional issues or only one issue.

Specific Matters for Comment

The AASB would particularly value comments on the following:

- 1 whether the proposals in this Exposure Draft are supported;
- 2 whether the amendments proposed in this Exposure Draft would result in a change from current practice, and, if so, why;
- 3 whether paragraph 4.1.2 of AASB 1038 should be retained;
- 4 whether, overall, the proposals would result in financial statements that would be useful to users;
- 5 whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, particularly any issues relating to:
 - (a) not-for-profit entities; and

- (b) public sector entities, including GAAP/GFS implications;
- 6 whether the proposals are in the best interests of the Australian economy; and
- 7 unless already provided in response to specific matters for comment 1 – 6 above, the costs and benefits of the proposals relative to the current requirements, whether quantitative (financial or non-financial) or qualitative.

**[DRAFT] ACCOUNTING STANDARD AASB
2013-XX**

***AMENDMENTS TO AASB 1038 ARISING FROM
AASB 10 IN RELATION TO CONSOLIDATION
AND INTERESTS OF POLICYHOLDERS***

Objective

- 1 The objective of this Standard is to remove the specific consolidation requirements from AASB 1038 *Life Insurance Contracts*, and thereby leave AASB 10 *Consolidated Financial Statements* as the sole source for consolidation requirements applicable to life insurer entities.

Application

- 2 This Standard applies to each entity that is:
- (a) a life insurer; or
 - (b) the parent in a group that includes a life insurer;
- when the entity:
- (c) is a reporting entity that is required to prepare financial reports in accordance with Part 2M.3 of the Corporations Act;
 - (d) is an other reporting entity and prepares general purpose financial statements; or
 - (e) prepares financial statements that are, or are held out to be, general purpose financial statements.
- 3 This Standard applies to annual reporting periods beginning on or after 1 January 2014.
- 4 This Standard shall be applied when AASB 10 is applied. This Standard may be applied to annual reporting periods beginning on or after 1 January 2005 but before 1 January 2014. When an entity applies this Standard to such an annual reporting period, it shall disclose that fact.

- 5 **The requirements specified in this Standard apply to the financial statements where information resulting from their application is material in accordance with AASB 1031 *Materiality*.**

Amendments to AASB 1038

- 6 The sub-heading above paragraph 4.1 is deleted and the heading above paragraph 4.1 is amended to read as follows:

4 Equity in a Shareholder-Owned Life Insurer

- 7 Paragraphs 1.1.1, 4.1 and 4.1.1 are deleted.

- 8 Paragraphs 4.2, 4.2.1 and 4.2.2 and the heading above paragraph 4.2 are deleted.

The full text of the paragraphs proposed to be deleted and the headings proposed to be deleted or amended is as follows:

- 1.1.1 This Standard applies to the consolidated financial statements of a group in relation to a life insurer subsidiary. Paragraph 4.2 is of particular relevance in this case.

4 Entity and Consolidation Issues

The life insurer entity

- 4.1 A life insurer shall recognise in its financial statements the assets, liabilities, income, expenses and equity of the entity, whether they are designated as relating to policyholders or to shareholders.**

- 4.1.1 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 statements. 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, govern 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.

...

Financial Statements of Groups that Include a Life Insurer Subsidiary

4.2 The consolidated financial statements of a group that includes a life insurer subsidiary shall recognise all of the assets, liabilities, income and expenses of that subsidiary, whether they are designated as relating to the policyholders or to the shareholders of that life insurer. The life insurance contracts, life investment contracts and assets of a life insurer subsidiary and its group recognised in the consolidated financial statements of a group shall be measured in accordance with this Standard.

4.2.1 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 controls the interests of both policyholders and shareholders and, accordingly, the consolidated financial statements of the group include all of those interests. The parent 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.

4.2.2 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 of a life insurer has no bearing on whether consolidated financial statements, prepared in accordance with paragraph 4.2, are required.

BASIS FOR CONCLUSIONS

This Basis for Conclusions accompanies, but is not part of, AASB 2013-XX.

Background

- BC1 This Basis for Conclusions summarises the Australian Accounting Standards Board's considerations in reaching the conclusions in the Exposure Draft. Individual Board members gave greater weight to some factors than to others.

Significant Issues

- BC2 In May 2011 the International Accounting Standards Board (IASB) issued IFRS 10 *Consolidated Financial Statements*¹ to replace the consolidation requirements in IAS 27 *Consolidated and Separate Financial Statements*². IFRS 10 also incorporates the guidance contained in SIC-12 *Consolidation – Special Purpose Entities*³. IFRS 12 *Disclosure of Interests in Other Entities*⁴, also issued in May 2011, replaced the disclosure requirements in IAS 27 *Consolidated and Separate Financial Statements*.
- BC3 Paragraph 4.1 of AASB 1038 currently requires a life insurer to recognise in its financial statements the assets, liabilities, income, expenses and equity of the entity, whether they are designated as relating to policyholders or to shareholders. The rationale given in paragraph 4.1.1 of AASB 1038 for this requirement is that the interests of policyholders and shareholders are intertwined and form the basis of a single entity, with the boundaries of the entity defined by control.
- BC4 The consolidation requirements in AASB 1038 were originally written in the context of AASB 1024 *Consolidated Accounts* (1992). Those requirements were considered to be consistent with AASB 127 *Consolidated and Separate Financial Statements* when it was made in 2004 (and subsequent amendments to the consolidation requirements of AASB 127 thereafter). Accordingly, AASB 1038 was not amended as a consequence of the issue of the original or subsequent amendments to AASB 127.

1 Incorporated into AASB 10 *Consolidated Financial Statements*. (As a consequence of issuing AASB 10, in August 2011, the AASB issued AASB 2011-7 *Amendments to Australian Accounting Standards arising from the Consolidation and Joint Arrangements Standards* which made amendments to AASB 1038.)

2 Incorporated into AASB 127 *Consolidated and Separate Financial Statements*.

3 Incorporated into Interpretation 112 *Consolidation – Special Purpose Entities*.

4 Incorporated into AASB 12 *Disclosure of Interests in Other Entities*.

- BC5 Although the consolidation requirements in AASB 10 and AASB 127 are both based on the concept of ‘control’, AASB 10 contains a revised definition of control. AASB 10 also contains requirements in relation to portions of an investee that are ‘deemed separate entities’, and on whether an investor controls the deemed separate entities.
- BC6 The Board is aware of the view that, under AASB 10, it is conceivable there could be circumstances in which policyholder interests are not controlled by a life insurer. In particular, it is conceivable that a ‘deemed separate entity’ that would meet the description in AASB 10 (often called a ‘silo’) could exist as a result of the characteristics of some insurance contracts for which the life insurer entity would need to assess whether the deemed separate entity is controlled (see paragraphs B76 to B79 of AASB 10).
- BC7 The Board is also aware of concerns that removing the consolidation requirements from AASB 1038 could lead to diversity in practice. Accordingly, the Board decided to issue this Exposure Draft to seek comment on the proposed removal of the explicit consolidation requirements in AASB 1038, thereby leaving AASB 10 as the sole source for consolidation requirements applicable to life insurer entities to avoid any potential conflict with AASB 10 – including in relation to the requirement relating to ‘uniform accounting policies for like transactions and other events in similar circumstances’ (see paragraph 19 of AASB 10). The proposals in this Exposure Draft are consistent with the Board’s policies of transaction neutral standards and of not issuing interpretations of IFRS (without first following the Interpretations Protocols).