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| Project | Insurance contracts |
| Topic | Presentation and disclosures |

Purpose

1. This paper seeks high-level comments from Working Group participants on some key issues on presentation and disclosure for insurance contracts.
2. The content of this paper is as follows:
 - (a) Presentation of net economic effect (paragraphs 4 - 6)
 - (b) Presentation of premiums as revenue or deposits (paragraphs 7 - 12)
 - (c) Disaggregating (changes in) the carrying amount of insurance liabilities (paragraphs 13 - 19)
 - (d) Discussion Paper Preliminary Views on Financial Statement Presentation (paragraphs 20 - 22)
3. This paper does not discuss:
 - (a) Whether other comprehensive income (OCI) could be used for recognising some changes in insurance.
 - (b) Whether insurance contracts should be unbundled if the contract contains more than one component.

This paper has been prepared by the technical staff of the IASB for the purposes of discussion at a public meeting of the IASB working group identified in the header of this paper.

The views expressed in this paper are those of the staff preparing the paper and do not purport to represent the views of any individual members of the Board or the IASB.

The meeting at which this paper is discussed is a public meeting but it is not a decision-making meeting of the Board. Official pronouncements of the IASB are published only after the Board has completed its full due process, including appropriate public consultation and formal voting procedures.

Presentation of net economic effect

4. The discussion paper on insurance contracts (Discussion Paper *Preliminary Views on Insurance Contracts*) proposes that an insurer would present the net economic effect of an insurance contract (paragraphs 122 f.). In other words, the contract is presented as a single net asset or liability, rather than being presented as a separate asset (relating to the cash inflows) and liability (relating to the cash outflows).
5. The Board took this position in its preliminary views, because it recognised the strong interdependency between the contract rights (cash inflows) and the expected claims and benefits (cash outflows). The different cash flow components of a contract are closely interrelated; the contract itself is designed and managed on a net basis. It also seems very difficult to transfer only the asset or liability part of the contract without transferring the remaining part as well.
6. Some may object to presenting an insurance obligation as a single liability number. The different characteristics of the cash flows could be blurred if only the net contract position is shown. The different characteristics of the cash flows represent different exposure to risks, which would not be shown in a net position. For example gross premium inflows might give an indication about new business activity, which would be hidden in a net presentation.

Presentation of premiums as revenue or deposits

7. The DP discussed whether premiums should be treated as premiums, as deposits, or as a mixture of revenue and deposits, but did not put forward specific proposals on this topic.
8. The DP considered four approaches:
 - (a) Present premiums for some or all contracts as revenue and the resulting payments to the policyholder as an expense.

- (b) Present premiums for some or all contracts as deposit receipts and present the resulting payments to the policyholder as repayments of the deposit (these payments would not appear in the statement of comprehensive income).
 - (c) Different insurance contracts use a different approach:
 - (i) Contracts driven mostly by service considerations present premiums as revenue.
 - (ii) Contracts that cover largely investment considerations show premiums as deposits.
 - (d) Unbundle some or all of the contracts into an insurance and deposit components and present those components accordingly.
9. Most respondents supported (a) presenting premiums as revenue, especially for non-life contracts. For life contracts, some saw merit in a margin presentation, particularly for life contracts; this approach builds on (b) presenting premiums as a deposit receipt (the income statement shows a release of margins earned rather than revenue, see paragraph 8 (b)).
10. Respondents generally opposed (d) unbundling, particularly if the various components of the contract are interdependent. They argued that the resulting measurement would not provide useful information and could only be achieved in a costly and arbitrary way.
11. If premiums are to be presented as revenue, two approaches are possible.
- (a) Premiums can initially be recognised as a liability (unearned part of the premium) and, when the premiums are earned, be presented as revenue. Revenue would be reported as the insurer is released from the obligation by performing under the contract. However, if the release of the insurance obligation includes effects of previous remeasurements, those effects could be presented on a separate line in the income statement. This approach would be consistent with the model proposed in the discussion paper on revenue recognition.

- (b) Another approach is to recognise premiums as revenue as they are received from the policyholder. Any corresponding increase in the insurance liability is recognised as an expense in the income statement. This approach results in recognising revenue on a written basis.

12. Consider for example a direct annuity. In many existing accounting models, the insurer would apply approach (b) of paragraph 8 by recognising the premium received as revenue on receipt and at the same time recognising (i) a liability and (ii) an expense (the increase in that liability). In contrast, the approach in paragraph 8 (a) would require the insurer to recognise a slice of the premium as revenue as it fulfils each slice of the performance obligation over the life of the contract.

Disaggregating (changes in) the carrying amount of insurance liabilities

Balance sheet

13. In developing an Exposure Draft for insurance contracts the boards have to consider the disaggregation of the insurance liability at reporting date. One natural way forward is disaggregating the insurance liability along the lines of the building blocks applied for measuring the liability, which for all of the candidates (except an unearned premium approach) could be applied in a way that it shows:
- (a) the expected present value of future cash flows, split into:
 - (i) cash inflows (premiums and other fees)
 - (ii) outflows (claims, benefits and expenses)
 - (b) a margin.
14. Some of the measurement approaches currently considered by the boards split the overall margin. For these candidates the margin could be further split into each of the margin components that flow from those approaches, for example a risk margin, service margin (if any) and a residual margin. We note that some

have concerns about disclosing some or all parts of the margin, particularly the risk margin, because they believe this might have unintended consequences.

15. The above information could be provided on the face of the balance sheet, in the disclosures or a mixture of both.
16. In addition to information on the insurance liability at the end of the reporting period, an overview of period-to-period changes (roll forward) may also provide useful information about the changes in the insurance liabilities during the period. Examples of elements that could be included in such a disclosure are:
 - (a) Inception of new contracts.
 - (b) Performance under the contract.
 - (c) Accretion of interest.
 - (d) Changes in estimates.

Income statement

17. The DP asked if the Board should require separately on the face of the income statement any specified components of the changes in the carrying amount of insurance liabilities. The level of required detail could mirror the possible reasons for changes, such as:
 - (a) Cash flows: inflows (premiums) and outflows (claims and benefits, handling costs).
 - (b) Expected changes: accretion of interest (“unwinding of the discount”) and release of margins.
 - (c) Differences between actual cash flows and previous estimates.
 - (d) Changes in circumstances: changes in discount rates, in estimates of cash flows, in effect of embedded options and guarantees, in margins because of changes in the quantity of risk or changes in the market price for bearing risk or providing other services

- (e) Policyholder participation: partly/ wholly discretionary, non-discretionary, unit-linking.
 - (f) Income or expense arising from reinsurance held.
 - (g) If applicable, the effects of business combinations and changes in foreign exchange rates.
18. If not specified on the face of the income statements, such items could be included in the disclosures.
19. Independently of the decision on the measurement attribute and of the treatment of acquisition costs, those costs and, if applicable, the related part of the premium could (perhaps should) be disclosed.

Discussion Paper Preliminary Views on Financial Statement Presentation

20. The discussion paper on financial statement presentation covers not only industry entities, but also financial services entities. Because financial services entities generate value mostly by managing financial assets and liabilities, financial assets and liabilities would, unlike in other businesses, be presented in the operating section, rather than investing or financing.
21. The Financial Statement Presentation project distinguishes essentially four categories that should be applied consistently over all the reports provided in the financial statements. These basic categories are:
- (a) Business:
 - (i) Operating
 - (ii) Investing
 - (b) Financing/ Equity
 - (c) Discontinued Operations
 - (d) Tax

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- (e) The financial statement presentation project team undertook field tests to analyse the usefulness of the requirements set out in the discussion paper. Amongst the companies under consideration were insurance companies. The analysis of the field tests is not completed yet.

Questions on presentation and disclosures issues

Comments and suggestions on the paper

Do you have any comments on or suggestions for the presentation and disclosure issues described in this paper:

- Presentation of net economic effect
- Presentation of premiums as revenue or deposits
- Disaggregating (changes in) the carrying amount of insurance liabilities
- Discussion Paper Preliminary Views on Financial Statement Presentation

Other comments and suggestions

Do you have any other comments or suggestions for presentation and disclosure?