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International Financial Reporting Standards

IASB/FASB project on Insurance Contracts

A technical update

IASC Foundation

The views expressed in this presentation are those of the presenter,
not necessarily those of the IASC Foundation or the IASB



IASB project on Insurance Contracts

- Project history and further planning
- Other relevant projects
- (Tentative) Decisions reached
- Outstanding issues



Project history

- IFRS 4 *Insurance Contracts*
 - first deliberations in 1997
 - standard issued in 2004 ('Phase I')
 - aimed at making only limited improvements
- Discussion Paper *Preliminary Views on Insurance Contracts* ('Phase II')
 - issued in 2007
 - further discussed since early 2008



Further planning

- FASB
 - joint project since 2008
 - intensified efforts
- Exposure Draft
 - expected for Q2 2010
- Standard
 - expected for Q2 2011



- Financial Instruments
 - Classification and measurement
- Revenue Recognition
 - Contracts with customers
- Liabilities (*Amendments to IAS 37 Provisions, Contingent Liabilities and Contingent Assets*)
 - Measurement of uncertain liabilities



Decisions reached

- Measurement approach
 - building blocks
 - margins
- Simplified approach
- Contract boundaries
- Acquisition costs
- Participating contracts
- Unbundling
- Reinsurance
- Policyholder accounting



Measurement approach

- Current measurement of an insurance contract
- Reflect insurer's fulfilment of the contract
- Building block approach
 - Four building blocks
- Combination of rights and obligations
- Presented on a net basis
- Not updated for risk of non-performance by insurer



Measurement approach continued

- Inputs: use all available information
 - Financial market variables: consistent with observable market prices
- Changes in insurance liabilities
 - IASB: profit or loss
 - [FASB: outstanding]



Building blocks

- Expected (probability-weighted) future cash flows
 - current estimates
 - expected to arise as the insurer fulfils the contract
 - policyholder behaviour/ future premiums
- Time value of money
 - characteristics of the liability
- Risk adjustment
- Amount eliminating day one differences ('Residual margin')
 - calibrated to the premium at inception



Risk adjustment

- Measure uncertainty associated with future cash flows
 - insurer's view of uncertainty
- Remeasured each reporting period
- Further guidance to be developed
 - Which techniques should be used?



Residual margin

- Allocation of ‘day-one difference’
- Specific guidance for releasing it to profit or loss
- Not adjusted for subsequent changes in estimates
 - Subsequent changes in estimates: income



Simplified approach

- Premium allocation model ('unearned premium')
- IASB: Required application
 - pre-claims liability
 - short-duration contracts (broadly)
- [FASB: outstanding]



Contract boundaries

- Where does an ‘existing contract’ end?
- Starting point of the analysis
 - insurer can cancel the contract, or
 - insurer can change the pricing of the contract
- More specific guidance
 - at a later stage



Acquisition costs

- Expense when incurred
- Not recognise any revenue (or income) at inception



Participating contracts

- Cash flows from participating features
 - cash flows like any other? [initial preference IASB]
 - or
 - recognise only to the extent a present obligation exists?
[initial preference FASB]
- Mutual insurers?



Unbundling

- Account for components of a contract as if they were separate contracts
- Required:
 - IASB: if a component is not interdependent with other components of an insurance contract
 - FASB: further clarification necessary
- Not permitted:
 - if components are interdependent
- Embedded derivatives?



Reinsurance

- Reinsurer- same measurement as all other insurers
- Cedant- same measurement as used for underlying direct insurance contracts
 - Follow-up (initial measurement, impairment)
- No offsetting
 - unless requirements for offsetting are met
- No derecognition of ceded contracts
 - unless obligation is discharged, cancelled or expired



Policyholder accounting

- Will not be addressed in the Exposure Draft
 - Except for reinsurance policyholder accounting



Outstanding issues

- Various follow-up issues, for example
 - risk adjustment
 - participating features
 - acquisition costs
- Performance reporting
- Unit-linked and universal life contracts
- Definition and scope
- Disclosures



Questions or comments?

Expressions of individual views by members of the IASB and its staff are encouraged. The views expressed in this presentation are those of the presenter. Official positions of the IASB on accounting matters are determined only after extensive due process and deliberation.

