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IASB continues its redeliberations

Decisions on insurance contracts revenue and other issues requiring further analysis

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Agenda

- Highlights of decisions from IASB meeting in April
- IASB staff recommendations and Board discussions
- The next steps and update on timetable

Highlights

- Education session on Insurance Contract Revenue on 24 April 2014.
- IASB meeting on 25 April 2014.
- Insurance contract revenue
  - Prohibition of including in the statement of comprehensive income (SOCI) premium amounts that are not consistent with commonly understood notions of revenue
  - Requirement to present insurance contract revenue in the SOCI
  - Retention of disclosures proposed in the 2013 ED related to volume information
- IASB decides on other issues requiring further analysis.

Overview of discussions

Accounting for insurance contracts

- The education session considered the mechanics for determining insurance contract revenue as proposed in the 2013 ED. The main focus was on 3 examples which illustrate the outcome of the revenue presentation proposals for a portfolio of life contracts.
- The IASB considered one of the five targeted proposals in its Exposure Draft issued in June 2013 (2013 ED), which deals with how entities would account for insurance contracts revenue.
- The IASB considered only insurance contracts that have no participating features.

Insurance contracts revenue

Should entities be prohibited from including in the statement of comprehensive income premium amounts that are not consistent with general notions of revenue?

Staff Recommendation

- Entities should be prohibited from presenting premium information in the statement of comprehensive income if that information is not consistent with commonly understood notions of revenue.

Insurance contracts revenue (contd.)

Benefits

- Consistency of revenue information between insurance and non-insurance contracts will reduce the risk of misinterpretation by non-specialist users.
- Improved comparability between all types of insurance contracts and insurance and non-insurance contracts.
- A more understandable format of financial statements will make insurance companies more transparent and accessible for non-specialist users.

Disadvantages

- Insurance contracts revenue does not provide information about volume sold in the period, and therefore does not provide a useful basis for assessing the size of the company, level of sales activity or growth.
- The investment component is an integral part of an insurance contract, therefore It would not be meaningful and would be excessively complex to separate it from the underlying insurance contract.

Insurance contracts revenue (contd.)

Staff comments and Board discussion

- The Staff commented that items currently included in the SOCI do not represent a consistent measure of revenue.
- Many IASB members commented on the presence of material deposit components in the premiums receivable from long term insurance contracts.
- They contemplated the merits of prohibiting premiums with significant deposit components being presented as revenue in the SOCI.
- The debate concluded with an assessment of the Staff recommendations against the general principles in IAS 1 and its application within the wider financial services industry (e.g. banks and asset managers).

IASB vote

- ➢ 13 Board members agreed with the Staff's recommendation, while 3 disagreed

Insurance contracts revenue

Is the cost of providing insurance contract revenue justified for all insurance contracts?

Staff Recommendation

- Entities should be ***required*** to present insurance contract revenue in the statement of comprehensive income, as proposed in paragraphs 56-59 and B88-B91 of the 2013 ED.

Fall-back recommendations

- If the IASB had not agreed with the Staff's assessment, 4 alternative approaches would have been considered to reduce the costs of requiring insurance contract revenue for all contracts. However, the Staff considered that each alternative has disadvantages in terms of comparability.

Insurance contracts revenue

Is the cost of providing insurance contract revenue justified for all insurance contracts?

Staff comments and Board discussion

- The Staff believe that the cost of excluding the investment component is justified for all contracts because it would be of great benefit to users, the biggest of which would be comparability with other industries.
- One Board member disagreed with this assessment because it would be difficult and expensive to separate the deposit component, and felt that the summarised margin approach may be a preferable alternative.
- The separation of deposit components attracted further debate which highlighted the need to treat these consistently between premiums and benefits/claims so that both revenue and expenses were consistently presented in the SOCI.
- A number of Board members questioned the approach to achieve consistency and whether the Staff were departing from a principle-based approach.

IASB vote

- 15 Board members agreed with the Staff's recommendation, while 1 disagreed.

Insurance contracts revenue (contd.)

Should we retain the disclosures proposed in the 2013 ED related to volume information?

Staff Recommendation

Entities should disclose the following:

- A reconciliation that separately reconciles the opening and closing balance of the components of the insurance contract asset or liability (paragraph 76 of the 2013 ED).
- A reconciliation from the premiums received in the period to the insurance contract revenue in the period (paragraph 79 of the 2013 ED).
- The inputs used when determining the insurance contract revenue that is recognised in the period (paragraph 81(a) of the 2013 ED).
- The effect of the insurance contracts that are initially recognised in the period on the amounts that are recognised in the statement of financial position (paragraph 81(b) of the 2013 ED).

Insurance contracts revenue (contd.)

Benefits

- Explains the insurance contract revenue recognised in the period.
- Provides volume information such as volume sold in the period, excluding expected premiums, related increase in obligation and expected profit.
- Provides reconciliation of the contract balances to show the change in margins that are recognised in the SOCI.

Disadvantages

- Some believe that disclosure of the reconciliation between the insurance contract revenue and existing volume measures is not useful, and some are concerned that reconciliations explaining insurance contract revenue recognised for the period are not necessary.
- These disclosures would increase the disclosure burden.

Insurance contracts revenue (contd.)

Staff comments and Board discussion

- The Staff stated that the first two disclosure requirements provided a reconciliation of revenue to cash inflows and disclosed the drivers of revenue, e.g. the margin and expenses.
- The other disclosures provided additional information about the underwriting activity and the expected cash inflows and acquisition costs of insurance contracts initially recognised in the period.
- The proposed disclosure requirements are very similar to that which would be required under the summarised margin approach, and will identify the impact of unlocking the CSM.
- The debate featured queries around the usefulness of premiums due as a KPI of an insurer’s activity (but not revenue). and why this was not required to be disclosed. The Staff responded that this would require premium due to be defined, and such a disclosure would add to the implementation costs.

IASB vote

➢ 14 Board members agreed with the Staff’s recommendation, while 2 disagreed.

Deloitte proposed amendments

- **We do not support the proposals for insurance revenue.**
- **We recommend the presentation of the summarised margin as presented in the 2010 ED.**
  - The insurance revenue proposal is inconsistent with the concept of accounting for insurance contracts as a bundle of rights and obligations
  - There is not the justification of a simplified method for departing from this key principle
  - The new revenue metric would not be the most faithful representation of the contribution that long duration contracts provide to financial performance
  - The co-existence of two different presentation requirements offers the most decision useful presentation of the contribution of short and long duration insurance contracts to an insurer's performance
  - Insurance revenue is not the volume information requested by investors.

Deloitte proposed amendments

- **We support the following disclosure requirement:**

- The effect of the insurance contracts that are initially recognised in the period on the amounts that are recognised in the statement of financial position

- Show separately the effect on the expected present value of future cash inflows, outflows, risk adjustment and CSM

- **We recommend that this disclosure is prominently disclosed in the notes.**

Project plan for non-targeted issues

Which issues should IASB consider in future meetings as requiring further analysis and may possibly need addressing?

Staff Recommendation

Issues identified as requiring further analysis in future meetings

- Fixed fee service contracts
- Significant insurance risk guidance
- Portfolio definition and unit of account
- Discount rate for long term contracts and unobservable market data
- Asymmetrical treatment of reinsurance contracts.
- Recognition of contracts acquired through the portfolio transfer or business combination
- Allocation pattern for the contractual service margin.

Project plan for non-targeted issues (contd.)

Which issues should IASB consider in future meetings as requiring further analysis and may possibly need addressing?

Issues *not* to be considered in future meetings

- Disclosures
- Premium allocation approach
- Combination of insurance contracts
- Contract boundary for specific contracts
- Unbundling - lapse together criteria
- Treatment of ceding commissions
- Discount rate - top-down and bottom-up approaches
- Tax included in the measurement
- Combining the contractual service margin with other comprehensive income

Project plan for non-targeted issues (contd.)

Which issues should IASB consider in future meetings as requiring further analysis and may possibly need addressing?

Staff comments and Board discussion

- The Staff considered that the unit of account, the discount rate for long-term contracts and the asymmetrical treatment of reinsurance contracts would require the greatest analysis.
- Board members suggested additional items to be reopened or introduced for the first time in the redeliberation process.
- One Board member asked whether it might be better to include contracts with participation features within the financial instruments standard. The Staff felt that the insurance contracts standard was a better fit, and this view was supported by a majority of the respondents to the 2013 ED.

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Project plan for non-targeted issues (contd.)

Staff comments and Board discussion (contd.)

- There were concerns about requiring the disclosure of the confidence level given the feedback from the actuarial profession as to it being impossible to calculate, lack of comparability and operational complexity. The Staff noted that similar comments had been presented to the IASB before the 2013 ED had been issued.
- The possibility to reassess the nature of the CSM as a component of the insurance liability was considered in its role in presenting unearned profit, its comparison with embedded value and its relevance at transition.
- None of these topics were approved for inclusion in the work plan.
- From the list of topics excluded, the Staff observed that concerns raised over the risk of inconsistent application of allowing top-down and bottom-up discount rates without abandoning the principles-based approach.

IASB vote

➢ 14 Board members agreed with the Staffs recommendation, while 2 disagreed.

The next steps and update on timetable

Future meetings

In future meetings the Staff plan to:

- Address the issues not targeted in the ED that the IASB tentatively decides to address.
- Consider the application of the model for non-participating contracts to contracts with participating features, including assessing any modifications that may be needed to reflect these features.
- Consider the transition requirements in the context of a near final model.

The next steps and update on timetable

Finalisation of the new standard

- The IASB expects that redeliberations of its proposals for the accounting for insurance contracts will be completed in 2014.
- The publication of a final Standard is expected in 2015.
- A more exact timetable will depend on decisions the IASB takes relating to the project plan for other issues.
- Decisions of the IASB become final only after completion of a formal ballot to issue a final standard

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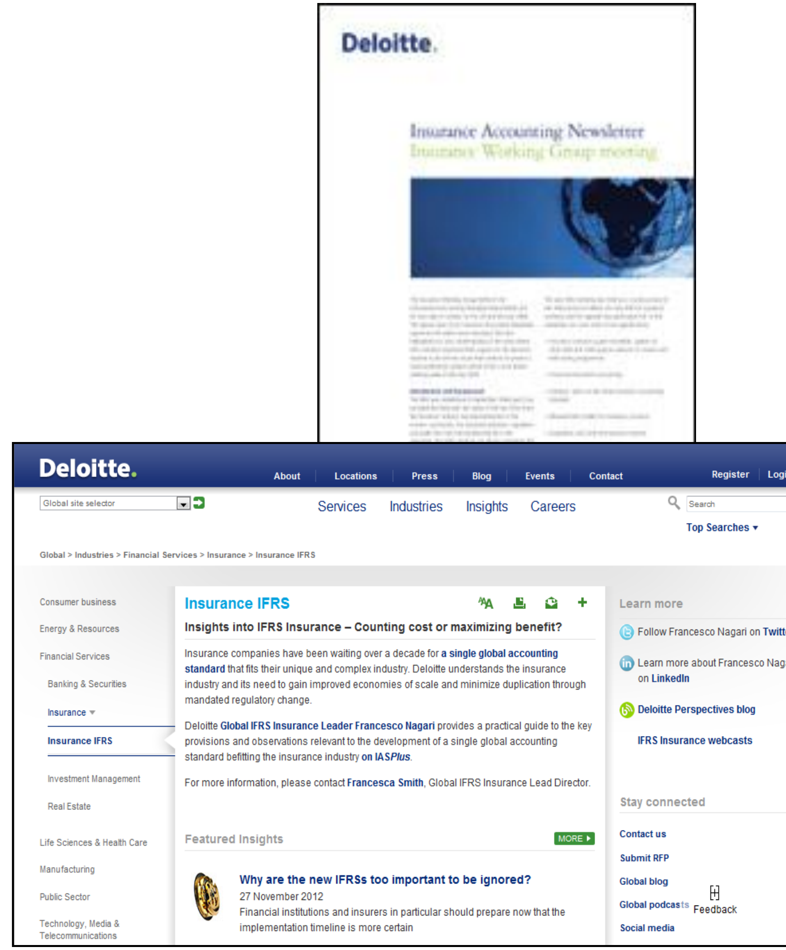

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