FINANCIAL ACCOUNTING SERIES

DISCUSSION PAPER

Issued: September 17, 2010
Comments Due: December 15, 2010

Comments for roundtable participants are requested
by November 30, 2010.

Preliminary Views on Insurance Contracts

This Discussion Paper is issued by the Financial Accounting Standards Board for public comment as a step preceding the development of an Exposure Draft of a proposed Accounting Standards Update.

Written comments should be addressed to:

Technical Director
File Reference No. 1870-100

Financial Accounting Standards Board
of the Financial Accounting Foundation

Responses from interested parties wishing to comment on the Discussion Paper must be *received* in writing by December 15, 2010. Interested parties should submit their comments by email to director@fasb.org, File Reference No. 1870-100. Those without email should send their comments to the “Technical Director—File Reference No.1870-100, FASB, 401 Merritt 7, PO Box 5116, Norwalk, CT, 06856-5116”. Do not send responses by fax.

All comments received constitute part of the FASB’s public file. The FASB will make all comments publicly available by posting them to its website and by making them available in its public reference room in Norwalk, Connecticut.

The FASB and IASB plan to hold several public roundtable meetings in December 2010. The purpose of those roundtable meetings is to listen to the views of, and obtain information from, interested stakeholders about this Discussion Paper and the IASB’s Exposure Draft, *Insurance Contracts*, which was issued July 30, 2010. The Board is seeking participants from a wide variety of stakeholders, including users, preparers, auditors, and others to ensure that broad input is received. Those who wish to participate in the roundtable in Norwalk, Connecticut, must notify the FASB by November 15, 2010, by sending an email to director@fasb.org and must submit comments on this Discussion Paper and/or the IASB’s Exposure Draft on insurance contracts in writing by November 30, 2010. Additionally, those who wish to participate in the roundtables in Europe or Asia must notify the IASB by November 15, 2010, by sending an email to roundtables@iasb.org and must submit comments on the IASB’s Exposure Draft and/or this Discussion Paper in writing by November 30, 2010. Roundtable meetings can accommodate a limited number of participants. Depending on the number of responses received, the Board may or may not be able to accommodate all requests to participate.

An electronic copy of the Discussion Paper is available on the FASB website.

Discussion Paper

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Preliminary Views on Insurance Contracts

Financial Accounting Standards Board
of the Financial Accounting Foundation
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Discussion Paper

Preliminary Views on Insurance Contracts

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SUMMARY

1. The purpose of this Discussion Paper is to summarize key aspects of the International Accounting Standards Board's (IASB) recent proposals in its Exposure Draft, *Insurance Contracts*, and to compare those proposals to:

a. Alternative preliminary views of the Board
b. Current guidance in Topic 944, Financial Services—Insurance, of the *FASB Accounting Standards Codification*™.

2. The Board seeks input from stakeholders on the overall approach and direction of the project, as well as on specific aspects of the IASB's and the FASB's views on accounting for insurance contracts (including reinsurance), even if the contracts are not issued by an insurance entity. The Board is particularly interested in stakeholders' views on how best to improve accounting for insurance contracts in the United States, whether through a fundamental and comprehensive reconsideration or through targeted improvements.

3 The FASB has been working with the IASB on a joint insurance project since the fourth quarter of 2008. On July 30, 2010, the IASB issued its Exposure Draft, which, when finalized, will replace, International Financial Reporting Standard (IFRS) 4, *Insurance Contracts*. The Board, however, decided to issue a Discussion Paper instead of an Exposure Draft of a proposed Accounting Standards Update for the following reasons:

a. The extent of the FASB's and the IASB's current accounting guidance for insurance contracts varies significantly. Existing U.S. generally accepted accounting principles (GAAP) comprehensively address accounting for insurance contracts by insurance entities, whereas IFRSs do not have comprehensive guidance. Whether or not the proposed approaches would improve current guidance is relative to significantly different starting points in U.S. GAAP and IFRSs. In addition, during their recent deliberations on the insurance contracts project, the Boards did not explicitly evaluate whether the model proposed in the IASB's Exposure Draft would represent an improvement to U.S. GAAP. Consequently, the FASB is seeking input from its stakeholders on this issue.
b. The Board has not determined whether one model or two models would result in more-useful information about insurance contracts. Current U.S. GAAP has separate models for long- and short-duration contracts with derivations within the long-duration model based on policy type. The Board would like additional input from stakeholders on whether different types of insurance contracts warrant different recognition, measurement, and presentation and, if so, what the criteria should be for determining which, if any, types of insurance contracts would use each model.

c. The Board is considering whether employer-provided health insurance should be included within the scope of the insurance contracts project and how recent U.S. healthcare reform may affect the application of the approaches described in this Discussion Paper and in the IASB's Exposure Draft.

Background

4. The Board contemplated whether insurance contracts should be included in the scope of the proposed Accounting Standards Update, *Revenue Recognition (Topic 605): Revenue from Contracts with Customers*. The Board noted that the proposed revenue recognition guidance might provide decision-useful information for some insurance contracts but not for all of them. Therefore, the Board decided to address accounting for insurance contracts in a separate project.

5. The Board's objective for the project is to improve U.S. GAAP for insurance contracts by developing high-quality guidance that addresses recognition, measurement, presentation, and disclosure. Specifically, the project is intended to improve, simplify, and achieve convergence of the financial reporting requirements for insurance contracts and to provide investors with decision-useful information.

U.S. GAAP for Insurance Contracts

6. The scope of U.S. accounting guidance is based on whether an entity providing insurance is an insurance company. U.S. GAAP has evolved as a result of new insurance products, terms, and features. Topic 944 requires application of different models depending on the nature of the insurance contract—one for short-duration insurance contracts (that is, for most property and liability contracts) and others for long-duration insurance contracts (that is, most life and annuity contracts).

7. Topic 944 has not been subject to comprehensive reconsideration by the Board before this project. Some of the more common elements of U.S. GAAP that some stakeholders note could be improved are highlighted below:

Current U.S. GAAP	**Desired Improvement**
Insurance entity orientation—Requirements do not apply to contracts issued by noninsurance entities even if contracts are economically and functionally equivalent to insurance contracts.	Regardless of the type of entity issuing the contracts, contracts that transfer significant insurance risk and contain identical or similar economic characteristics should be accounted for in a similar manner.
Definition of an insurance contract—Insurance contracts under U.S. GAAP are those written by insurance entities that indemnify the policyholder against loss or liability. A notion based on indemnification generally limits the claim to the amount of the loss.	A uniform definition of an insurance contract should be developed. That definition should use *compensation* rather than *indemnification* to define the insurance contract benefit. Compensation is a broader notion than indemnification and would be less likely to limit the claim payment to the loss.
Deferral of acquisition costs—Costs that vary with and are primarily related to the acquisition of insurance contracts may be deferred and subsequently amortized. Diversity in practice exists with respect to which costs may be deferred. Recently, the Emerging Issues Task Force (EITF) reached a final consensus to narrow the types of costs that may be capitalized. Specifically, the new model aligns the recognition of deferred acquisition costs with the accounting for loan origination costs in Subtopic 310-20, Receivables—Nonrefundable Fees and Other Costs.	If targeted improvements are made to current U.S. GAAP (rather than amended by the proposed model being discussed jointly with the IASB), some have said the EITF final consensus may adequately improve the accounting model for acquisition costs relating to insurance contracts. Others have said that all acquisition costs should be expensed as incurred to be generally consistent with the accounting guidance for costs to acquire contracts that generate revenue in numerous other Topics within U.S. GAAP.
Assumptions for traditional long-duration contracts—The assumptions used to calculate long-duration contract policyholder benefits are locked in (that is, they are not updated unless the existing contract liabilities, together with the present value of future gross premiums, become insufficient to cover the present value of future benefits to be paid to or on behalf of the policyholders and to recover unamortized acquisitions costs).	To reflect the risks and uncertainties inherent in long-duration contracts, some or all assumptions should be reevaluated and updated at each reporting period to reflect all available information.

Current U.S. GAAP	Desired Improvement
Discount rate for traditional long-duration contracts—Assumptions for discounting of liabilities on traditional long-duration contracts are based on the estimated investment yields (net of related investment expenses) expected at the contract issue date.	The discount rates used to measure the contract liabilities should be based on current rates that reflect the characteristics of the liabilities rather than the invested assets related to those liabilities.
Lack of discounting of liabilities for short-duration contracts—Most liabilities for short-duration contracts are not discounted even though the expected claims settlement (payment) period may extend for many years on some contracts.	Measurement of all contract liabilities should be discounted at current rates to reflect the time value of money, if material.

International Accounting Standards for Insurance Contracts

8. In contrast to U.S. GAAP, IFRSs do not contain comprehensive guidance on accounting for insurance contracts. The lack of uniform international accounting standards results in inconsistent accounting practices. Consequently, users of financial statements of international insurers have indicated that accounting for insurance contracts is difficult to understand and does not provide sufficient decision-useful information about an insurer's financial position and financial performance.

History of the Project

9. In 2002, the IASB decided to address accounting for insurance contracts in a two-phase project. The first phase of the project was completed in May 2004 with the issuance of IFRS 4, which provided temporary guidance for insurers adopting IFRSs in 2005. IFRS 4 made limited improvements to accounting practices for insurance contracts, permitted a wide variety of practices to continue, and avoided major changes that might be reversed upon completion of the second phase.

10. As part of the second phase of the project, in May 2007, the IASB issued a Discussion Paper, *Preliminary Views on Insurance Contracts*, which focused on developing a comprehensive accounting model for an insurer's rights and obligations (insurance assets and liabilities) arising from insurance activities.

11. In August 2007, the Board issued an Invitation to Comment, *An FASB Agenda Proposal: Accounting for Insurance Contracts by Insurers and Policyholders*, *Including the IASB Discussion Paper,* Preliminary Views on Insurance Contacts, which included the IASB's Discussion Paper. The Board received 45 comment letters in response to the Invitation to Comment, which led

to its decision in October 2008 to participate in the project jointly with the IASB. Since then, the Boards have held more than 20 meetings to discuss various proposals to develop a common standard for insurance contracts. Although the project on insurance contracts is a joint project, it is not part of the Boards' Memorandum of Understanding that was issued to acknowledge their commitment to the development of high-quality, compatible accounting standards and further the convergence of U.S. GAAP and IFRSs.

12. The IASB published an Exposure Draft on financial reporting for insurance contracts on July 30, 2010, which, when finalized, will replace IFRS 4. In developing the IASB's Exposure Draft, most of the discussions about the proposed insurance accounting approaches were held jointly with the FASB. While the Boards reached common decisions in many areas, they reached different conclusions in others. Those differences, as well as how they compare to existing U.S. GAAP, are highlighted in the appendix of this Discussion Paper.

13. Some Board members prefer the IASB's proposed approach; however, the majority prefers an alternative approach. Regardless of Board members' individual views and uniform commitment to convergence, the Board determined that additional information was needed about whether the possible new accounting guidance in this Discussion Paper would represent a sufficient improvement to U.S. GAAP to justify issuing new guidance.

14. Because some of the IASB's proposals are similar to provisions in current U.S. GAAP (see the appendix), the Board is soliciting input from stakeholders on the advantages and disadvantages of pursuing a comprehensive reconsideration of insurance accounting versus making targeted improvements to current U.S. GAAP, primarily on the basis of the items discussed in paragraph 7.

INVITATION TO COMMENT

15. The Board invites comments on all matters in this Discussion Paper. Comments are most helpful if they:

a. Respond to the questions as stated
b. Indicate the specific paragraph or paragraphs to which the comments relate
c. Contain a clear rationale
d. Describe any alternative that the Board should consider.

16. The Board is interested in whether the IASB's proposed approach or the FASB's preliminary views would represent a sufficient improvement to existing U.S. GAAP to justify issuing new guidance. The Board is interested in whether the proposals would improve transparency, comparability, and decision usefulness. Finally, the Board is interested in information about the possible benefits of using information provided by the proposed new reporting model as well as the operational issues and costs associated with implementing the proposals.

17. Respondents need not comment on all the questions and are encouraged to comment on any additional issues, as well as questions included in the IASB's Exposure Draft.

18. Comments on this Discussion Paper are due in writing by December 15, 2010. Although the Board issued a Discussion Paper and the IASB issued an Exposure Draft, feedback received by the Boards on both documents will be discussed as part of redeliberations in joint meetings, which are anticipated to commence in January 2011. Thereafter, the Board will decide whether to issue new guidance to improve U.S. GAAP for insurance contracts.

Public Roundtable Meetings

19. The Boards plan to hold several public roundtable meetings in December 2010. The purpose of these roundtable meetings is to listen to the views of, and obtain information from, interested stakeholders about this Discussion Paper and the IASB's Exposure Draft. The Board will seek participation in the roundtables from a wide variety of stakeholders, including users, preparers, auditors, and others to ensure that broad input is received. Those who wish to participate in the roundtable in Norwalk, Connecticut, must notify the FASB by November 15, 2010, by sending an email to director@fasb.org and must submit comments on this Discussion Paper and/or the IASB's Exposure Draft on insurance contracts in writing by November 30, 2010. Additionally, those who wish to participate in the roundtables in Europe or Asia must notify the IASB by November 15, 2010, by sending an email to roundtables@iasb.org and must submit comments on the IASB's Exposure Draft and/or this Discussion Paper in writing by November 30,

2010. Roundtable meetings can accommodate a limited number of participants. Depending on the number of responses received, the Boards may or may not be able to accommodate all requests to participate.

QUESTIONS FOR RESPONDENTS

20. For ease of use, all of the questions for respondents in this Discussion Paper are presented here. Each question also is repeated in the section to which it relates.

Definition and Scope

1. Are the proposed definitions of *insurance contract* and *insurance risk* (including the related guidance) understandable and operational?
2. If the scope of the proposed guidance on insurance contracts is based on the definition of an insurance contract rather than on the type of entity issuing the contract, would financial reporting be improved?
3. Do you agree with the proposed scope exclusions? Why or why not?
4. Should benefits that an employer provides to its employees that otherwise meet the definition of an insurance contract be within the scope of the proposed guidance? Why or why not?
5. The Board's preliminary view is that participating investment contracts should not be accounted for within the proposed model for insurance contracts but, rather, should be included in the scope of the proposed model for accounting for financial instruments. Do you agree? Why or why not?
6. Do you support the approach for determining when noninsurance components of contracts should be unbundled? Why or why not?

Recognition and Measurement

7. Do you agree with the use of the probability-weighted estimate of net cash flows to measure insurance contracts? Does that approach faithfully represent the economics of insurance contracts? Is it an improvement over existing U.S. GAAP?
8. Do you think that an entity's estimate of the net cash flows should include a risk adjustment margin?
9. Is the objective of the risk adjustment margin understandable? If so, do you think that the techniques for estimating the risk adjustment margin (see paragraph 52(b)), faithfully represent the maximum amount that the

insurer would rationally pay to be relieved of the risk that the ultimate fulfillment cash flows exceed those expected?

10. Do you think that the risk adjustment margin would be comparable for entities that are exposed to similar risks?

11. Do you agree with the description of cash flows that should be included in the measurement of an insurance contract? Is the proposed guidance operational?

12. Do you agree that the carrying amount of all insurance contracts should be discounted if the effect is material? Do you agree with the proposed guidance on the discount rate that should be used to measure the carrying amount of insurance contracts? If not, which discount rate should be used?

13. Do you think that acquisition costs should be included as one of the cash flows relating to the contract? If not, how would you account for acquisition costs?

14. Do you agree that acquisition costs included in the cash flows used in the measurement of the insurance contract should be limited to those that are incremental at the individual contract level? If not, which acquisition costs, if any, would you include in the measurement of the insurance contract?

15. Do you agree with the use of either the composite margin approach or two-margin approach to measure the net insurance contract? Does either approach faithfully represent the economics of insurance contracts? Is either approach an improvement over the measurement used in current U.S. GAAP?

16. Do you think that the composite margin should be recognized in earnings in subsequent periods using the ratio described in paragraph 83? If not, how would you recognize the composite margin in earnings?

17. Do you agree that interest should not be accreted on the composite margin? Why or why not?

18. Do you think that all insurance contracts should be recognized and measured using one approach or that some insurance contracts should be recognized and measured using an alternative approach (for example, the modified approach)? Why or why not?

19. If an alternate approach is required for some insurance contracts, what recognition, measurement, and presentation provisions should be applied (including those items noted in paragraph 106)?

20. Do both the building-block approach and the modified approach (with the latter approach applied only to certain short-duration contracts) produce relevant and decision-useful information? Why or why not?

21. How should the scope of insurance products for each approach be defined (for example, duration of coverage period, duration of claims payment period, or type of insurance)?
22. Are there specific types of insurance contracts for which the approaches would not provide decision-useful information?
23. What are the implications of the recent U.S. healthcare reform to the application of the proposed contract boundary principle, including whether health insurance contracts written under the new reforms would meet the conditions in the proposed guidance to be accounted for under the modified approach?
24. What other changes should be considered to both improve and simplify U.S. GAAP for short- and long-duration insurance contracts?
25. What are the incremental costs of adopting the alternatives described in this Discussion Paper? Please separately describe one-time costs and ongoing costs.

Reinsurance

26. The scope of the proposed guidance includes reinsurance contracts that an insurer issues or acquires. However, insurance contracts held directly by other policyholders would be excluded from the scope of the proposed guidance. Do you agree with this exclusion? Why or why not?
27. Should there be symmetry between the recognition and measurement of reinsurance contracts and the underlying contract ceded?

Presentation and Disclosure

28. The margin presentation approach highlights the changes in the insurance liability, rather than the current approach in U.S. GAAP, which presents, among other items, premium revenues, benefits paid, operating costs, and changes in loss estimates. Would this change improve your understanding of the performance of an entity that provides insurance (for some types of insurance or for all)? Please explain.
29. Should insurance contracts measured under the building-block approach be presented using a margin presentation approach or a premium presentation approach that would require a true-up amount as described in paragraph 119 (for example, the written allocation presentation approach or the allocated premium presentation approach)?
30. Should short- and long-duration (or nonlife and life) contracts be

presented in a similar manner even if such contracts are measured under different approaches?

31. Do you agree with the proposed disclosures in the IASB's Exposure Draft? Why or why not? If not, what would you recommend and why?

Additional Question for Respondents

32. After considering your views on the specific issues contained in this Discussion Paper and the IASB's Exposure Draft, what do you think would represent the most appropriate improvement to U.S. GAAP?

    a. Pursue an approach based on the IASB's Exposure Draft?
    b. Pursue an approach based on the IASB's Exposure Draft with some changes? Please explain those changes.
    c. Pursue an approach based on the Board's preliminary views in this Discussion Paper?
    d. Pursue an approach based on the Board's preliminary views in this Discussion Paper with some changes? Please explain those changes.
    e. Make targeted changes to address specific concerns about current U.S. GAAP (for example, items included in paragraph 7)? Please describe those changes.

DEFINITION AND SCOPE

Definition of an Insurance Contract

21. Topic 944 does not explicitly define an insurance contract. Instead, the application of U.S. GAAP for insurance contracts depends on whether the entity writing the contract is an insurer.[1] As a result, contracts that are economically and functionally equivalent to insurance contracts do not apply the same accounting if not issued by an insurer. For example, some financial guarantees issued by banks or other noninsurance entities are excluded from applying Topic 944.

22. To improve comparability, the proposed accounting requirements would apply to most insurance contracts (as defined below), regardless of the type of entity issuing the contract. With that objective, the Boards jointly agreed on the following definition of an *insurance contract*:

> A contract under which one party (the insurer[2]) accepts significant insurance risk from another party (the policyholder[3]) by agreeing to compensate the policyholder if a specified uncertain future event (the insured event[4]) adversely affects the policyholder.

23. That proposed definition focuses on the unique feature of insurance contracts, namely insurance risk. As noted in the IASB's Exposure Draft, insurance risk refers to risk that the insurer accepts from the policyholder. As a component of the definition of an insurance contract, *insurance risk* is proposed to be defined as follows:

> Risk, other than financial risk,[5] transferred from the holder of a contract to the issuer.

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[1]For ease of reference, this Discussion Paper describes any entity that issues an insurance contract as an *insurer*, whether or not the issuer is regarded as an insurer for legal or supervisory purposes.

[2]An *insurer* would be defined as the party that has an obligation under an insurance contract to compensate a policyholder if an insured event occurs.

[3]A *policyholder* would be defined as a party that has a right to compensation under an insurance contract if an insured event occurs.

[4]An *insured event* would be defined as an uncertain future event that is covered by an insurance contract and creates insurance risk.

[5]*Financial risk* would be defined as the risk of a possible future change in one or more of the following: specified interest rate; financial instrument price; commodity price; foreign exchange rate; index of prices or rates; credit rating or credit index; or other variable, provided in the case of a non-financial variable that the variable is not specific to a party to the contract.

24. Additionally, a contract is an insurance contract only if it transfers significant risk. Paragraph B24 of the IASB's Exposure Draft includes further guidance on whether insurance risk is significant:

> Insurance risk is significant if, and only if, an insured event could cause an insurer to pay significant additional benefits in any scenario, excluding scenarios that lack commercial substance (ie have no discernible effect on the economics of the transaction). If significant additional benefits would be payable in scenarios that have commercial substance, the condition in the previous sentence can be met even if the insured event is extremely unlikely or even if the expected (ie probability-weighted) present value of contingent cash flows is a small proportion of the expected present value of all the remaining cash flows from the insurance contract.

25. Examples of contracts that would or would not be insurance contracts are outlined in paragraphs B18–B22 of the IASB's Exposure Draft. In addition, guidance about whether insurance risk is significant is discussed in paragraphs B23–B31 of the IASB's Exposure Draft.

Scope

26. All insurance contracts (life and nonlife, and reinsurance[6]) would be accounted for under the proposed model(s) regardless of the type of entity issuing the contract, which differs from current U.S. GAAP (see paragraph 7).

27. The proposed definition of an insurance contract also would apply to certain contracts that provide coverage against credit defaults. Those contracts can have various legal forms and are included in the scope of the proposed guidance if the entity issuing the contract accepts significant insurance risk. For example, the entity issuing the contract would accept significant insurance risk if it is required to reimburse the holder for a loss incurred when a debtor fails to make payments according to the original or modified terms of a debt instrument. The IASB has termed those contracts *financial guarantee contracts* (see paragraphs BC193–BC197 of the IASB's Exposure Draft).

Scope Exclusions

28. The following would be excluded from the scope of the proposed guidance:

   a. Product warranties issued by a manufacturer, dealer, or retailer. (See Topic 460, Guarantees.)

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[6]A *reinsurance contract* is a type of insurance contract. Accordingly, all references to insurance contracts also apply to reinsurance contracts.

b. Employers' assets and liabilities under employee benefit plans and retirement benefit obligations reported by defined benefit retirement plans (see paragraphs 30–32).
c. Contractual rights or contractual obligations that are contingent on the future use of, or right to use, a nonfinancial item (for example, some license fees, royalties, contingent lease payments, and similar items). (See Topic 840, Leases, and Topic 350, Intangibles—Goodwill and Other.)
d. Residual value guarantees provided by a manufacturer, dealer, or retailer, as well as a lessee's residual value guarantee embedded in a finance lease. (See Topics 840 and 350.)
e. Fixed-fee service contracts that have the provision of services as their primary purpose, but that expose the service provider to risk because the level of service depends on an uncertain event. (See paragraphs BC208–BC209 of the IASB's Exposure Draft.) However, an insurer would apply the proposed guidance to insurance contracts in which the insurer provides goods or services to the policyholder to compensate the policyholder for insured events.
f. Contingent consideration payable or receivable in a business combination. (See Topic 805, Business Combinations.)
g. Direct insurance contracts in which the entity is the policyholder. However, a cedant would apply the proposed guidance to reinsurance contracts that it holds. (See paragraphs 108–110 for further discussion.)

29. Additionally, the Board would exclude financial instruments that contain discretionary participation features from the scope of the proposed guidance. However, the IASB would include those instruments in the scope of its proposed guidance. (See paragraphs 33–38 for further discussion.)

Employer-Provided Insurance

30. As noted in paragraph 28(b), all employers' assets and liabilities under employee benefit plans would be excluded from the scope of the proposed guidance. Under IFRSs, that exclusion would include, among other items, health insurance provided by an employer. However, the Board questions whether those particular arrangements should be excluded from the scope of the proposed guidance for U.S. GAAP.

31. While providers of insurance receive distinct premiums, the premiums to pay for employer-provided coverage may be deducted from employees' salaries either implicitly or explicitly. Some have said that those insurance activities should be within the scope of the proposed guidance. However, others noted that employer-provided insurance represents compensation expense and, therefore, should not be considered an insurance contract.

32. Some stakeholders are concerned about how the recent U.S. healthcare reform may affect all health insurance arrangements. For example, some stakeholders question how such reforms may affect the application of the proposed contract boundary principle (see paragraphs 46 and 47) and whether health insurance contracts written by employers under the new reforms would be eligible for the modified approach (see paragraphs 94–107).

Financial Instruments with Discretionary Participation Features

33. Under both the FASB's preliminary views and the IASB's proposed guidance, a participating insurance contract would be included in the scope of the proposed new guidance. Those contracts provide insurance coverage to the policyholder as well as contractual rights to participate in the performance of the same insurance contracts, the same pool of assets, or the profit or loss of the same company.

34. However, as noted in paragraph 29, the Boards' opinions diverged for financial instruments with discretionary participation features[7] (that is, participating investment contracts). Those instruments do not meet the proposed definition of insurance contracts because they do not transfer significant insurance risk to the insurer.

35. However, the IASB proposes to include those investment contracts in the scope of its proposed guidance if such contracts share in the performance of the same pool of assets as participating insurance contracts. That condition would amend the definition of a *discretionary participation feature* in IFRS 4. Additionally, because participating investment contracts do not transfer significant insurance risk, the IASB proposes the following modifications to the model for financial instruments with discretionary participation features:

a. Establish the contract boundary principle on the presence of the discretionary participation feature rather than on the existence of insurance risk.
b. Recognize the residual margin in earnings on the basis of the pattern of the provision of asset management services rather than on the pattern of claims and benefits.

36. The IASB notes the following advantages of treating participating investment contracts similar to participating insurance contracts instead of as financial instruments:

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[7] A *discretionary participation feature* would be defined as a contractual right to receive, as a supplement to guaranteed benefits, additional benefits as described in Appendix A of the IASB's Exposure Draft. Furthermore, *guaranteed benefits* would be defined as payments or other benefits to which a particular policyholder or investor has an unconditional right that is not subject to the contractual discretion of the issuer.

a. Participating investment contracts and participating insurance contracts often are linked to the same underlying pool of assets. Using the same approach for both types of contracts would provide more relevant information for users and simplify the accounting.
b. Both types of contracts often share features more similar to insurance contracts (for example, long maturities, recurring premiums, and high acquisition costs) than to financial instruments. The IASB's intent was to develop a model for insurance contracts to provide useful information about contracts containing those features.
c. Participating investment contracts contain complex, interdependent options and guarantees that would be bifurcated under current and proposed requirements for financial liabilities. However, applying different accounting methods to the separate components may not provide a faithful representation of the entire contract, resulting in less understandable information.

37. In contrast, the Board said that such contracts should not be within the scope of the proposed insurance guidance for the following reasons:

a. Participating investment contracts do not meet the definition of an insurance contract because they do not transfer significant insurance risk to the insurer. Therefore, they should be treated as financial instruments.
b. Applying the insurance model to contracts that do not meet the definition of an insurance contract would cause additional complexities—for example, the need to isolate those contracts from other investment contracts and develop a separate contract boundary principle.
c. In some jurisdictions, investment contracts with discretionary participation features form a substantial part of an insurer's business. Including a substantial volume of noninsurance contracts in the scope of the proposed insurance guidance may cause the model to take on the character of an industry-specific model.
d. Similar contracts issued by noninsurer financial institutions are accounted for under current guidance on financial instruments. Accounting for similar contracts using different accounting models would reduce comparability and add complexity.

38. Therefore, in the Board's view, participating investment contracts would be accounted for in accordance with the guidance on financial instruments.

Questions for Respondents

1. Are the proposed definitions of *insurance contract* and *insurance risk* (including the related guidance) understandable and operational?

2. If the scope of the proposed guidance on insurance contracts is based on

the definition of an insurance contract rather than on the type of entity issuing the contract, would financial reporting be improved?

3. Do you agree with the proposed scope exclusions? Why or why not?

4. Should benefits that an employer provides to its employees that otherwise meet the definition of an insurance contract be within the scope of the proposed guidance? Why or why not?

5. The Board's preliminary view is that participating investment contracts should not be accounted for within the proposed model for insurance contracts but, rather, should be included in the scope of the proposed model for accounting for financial instruments. Do you agree? Why or why not?

Unbundling

39. Insurance contracts may provide the policyholder with goods, services, or investment opportunities other than insurance coverage. The Boards agree that the noninsurance elements of such contracts would be separated (unbundled)[8] from the insurance elements on the basis of the following principle (similar to that described in paragraph 8 of the IASB's Exposure Draft):

> If a component is not closely related to the insurance coverage specified in a contract, an insurer would account for that component as if it were a separate contract and apply the relevant standard to that component (that is, the insurer would unbundle that component).

40. The unbundling principle would not require an exhaustive search for noninsurance components in every insurance contract. Rather, the purpose would be to assist investors in understanding an insurance contract with one or more components while improving comparability between entities across industries. To assist insurers in applying the proposed unbundling requirements, the Boards identified the following common examples of components that would not be closely related to the insurance coverage:

a. An investment component reflecting an account balance that meets both of the following conditions:
    1. The account balance is credited with an explicit return (that is, it is not an implicit account balance, for example, derived by discounting an explicit maturity value at a rate not explicitly stated in the contract).
    2. The crediting rate for the account balance is based on the investment performance of the underlying investments—namely,

[8] *Unbundling* would be defined as accounting for the components of a contract as if they were separate contracts, according to their nature.

a specified pool of investments for unit-linked contracts, a notional pool of investments for index-linked contracts, or a general account pool of investments for universal life contracts. That crediting rate must pass on all investment returns (net of contract fees and assessments) to the individual policyholder. Contracts that are based on the investment performance of the underlying investments and pass on all investment returns (net of contract fees and assessments) may specify conditions under which there may be a minimum guarantee. However, contracts may not specify a maximum return because such a condition would indicate that all investment returns are not passed through to the policyholder.

b. An embedded derivative that is separated from its host contract in accordance with existing bifurcation guidance (see Topic 815—Derivatives and Hedging).
c. Contractual terms relating to goods and services that are not closely related to the insurance coverage but that have been combined in a contract with that coverage.

41. In the Boards' view, the benefits of unbundling noninsurance elements outweigh the added costs for the following reasons:

a. Transparency—Unbundling would provide insight into the components of an insurance contract that do not respond to changes in circumstances in the same manner as components affected by insurance risk.
b. Comparability—The result of unbundling is that an insurer would account for a noninsurance component of a contract in the same manner as another entity with a separate, but otherwise identical, contract. Thus, users of financial statements would be able to compare the risks undertaken by different entities, regardless of the entities' type of business.

42. The Boards propose to disallow unbundling when it would not be required because doing so would undermine comparability and likely would not provide more decision-useful information.

Question for Respondents

6. Do you support the approach to determine when noninsurance components of contracts should be unbundled? Why or why not?

RECOGNITION AND MEASUREMENT

43. The IASB's Exposure Draft proposes a comprehensive approach for all insurance contracts issued by insurers, except those short-duration contracts to which a modified approach would apply (see paragraph 96). Under the IASB's Exposure Draft and the FASB's preliminary views, the carrying amount of an insurance contract would not be based on a fair value measurement as defined in U.S. GAAP or IFRSs. Instead, an insurance contract would be measured on the basis of the rights and obligations created by that contract that result in a series of cash inflows (for example, premiums and deposits) and outflows (for example, benefits, claims, and expenses). Insurers would measure insurance contracts, in part, on the basis of the difference between net cash inflows and outflows expected to arise over the remaining coverage and claims handling periods.[9] The assumptions used to measure the insurance contracts would be updated each reporting period.

Recognition

44. An insurer would recognize an insurance obligation when it becomes a party to the contract, which is defined as the earlier of the date on which the insurer is bound by either of the following:

a. The terms of the contract
b. Initial exposure to risk under the contract (that is, when the insurer can no longer withdraw from its obligation to provide insurance coverage to the policyholder for insured events and when it no longer has the right to reassess the risk of the particular policyholder and, as a result, cannot set a price that fully reflects that risk).

45. An insurer could become a party to an insurance contract before the coverage period starts. In many cases, the measurement of insurance contracts does not change materially after initial recognition and before the start of the coverage period. During that time, the measurement of the insurance contract would be updated only for cash received or paid, the accretion of interest, changes in estimates of cash flows, and discount rates. An insurer would begin to recognize the residual or composite margin in earnings after the coverage period begins.

[9]The *coverage period* would be defined as the period during which the insurer provides coverage for insured events. The *claims handling period* would be defined as the period during which the insurer investigates and pays claims.

Initial Measurement

Contract Boundaries

46. The boundary of an insurance contract would distinguish the net cash flows that relate to existing insurance contracts from those that relate to future insurance contracts. The boundary of an insurance contract would be the point at which an insurer either:

   a. Is no longer required to provide coverage; or
   b. Has the right or the practical ability to reassess the risk of the policyholder and, as a result, can set a price that fully reflects that risk.

47. The measurement of the net insurance contract would include premiums and other cash flows resulting from those premiums if either:

   a. The insurer can compel the policyholder to pay the premiums and other cash flows; or
   b. The premiums and other cash flows are within the boundary of the contract.

Accounting for Policyholder Behavior

48. Policyholder options, forwards, and guarantees related to existing contracts would be measured using the expected value of the net cash flows (to the extent that the cash flows are within the boundaries of the existing contract). Therefore, if a policy is expected to be renewed, the insurer would not record the liability at the cash surrender value (deposit floor or minimum liability), but rather, would estimate the life of the policy and the cash flows relevant to that time frame.

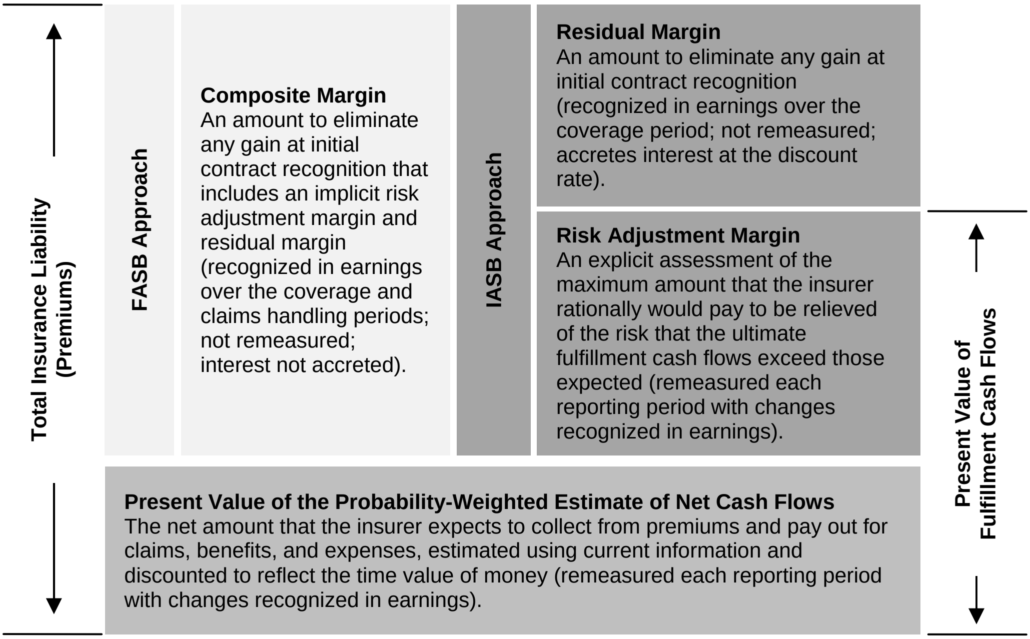
49. Policyholder options, forwards, and guarantees that do not relate to the existing insurance coverage would be excluded from the measurement of the contract. Those instruments would be recognized and measured as either new insurance contracts or other standalone instruments according to their nature.

Building-Block Approach

50. The proposed measurement approach (*the building-block approach*) would depict a current assessment of an insurance contract and would provide information about the main drivers of profitability in the current period. The Boards agree on the first building block—the present value of the probability-weighted estimate of net cash flows. However, the majority of the members of the Boards have differing views about whether an explicit risk adjustment margin and a residual margin (IASB approach) or whether a composite margin (FASB approach) should be added to the present value of the probability-weighted estimate of net cash flows to reflect the profit and ongoing measurement of the

contract. The diagram below illustrates the key elements of the building-block approach and highlights the differences between the IASB's *two-margin approach* and the FASB's *composite margin approach*.

The Building Blocks of the Proposed Approaches



51. Under the Board's preliminary view of the building-block approach (*the composite margin approach*), risk and uncertainty would be reflected implicitly through a single composite margin rather than explicitly through a separate risk adjustment margin as in the IASB's two-margin approach. Differences in measurement between the two views of the building-block approach do not arise at initial recognition of an insurance contract because both views calibrate the residual margin and composite margin to the present value of consideration received or receivable from the policyholder (unless the contract is onerous upon initial recognition).

52. Under the IASB's proposed building-block approach (*the two-margin approach*), an insurer would measure an insurance contract initially as the sum of the following:

a. The present value (unbiased and probability-weighted estimate) of the cash outflows less cash inflows that are expected to arise over the remaining coverage and claims handling periods.
b. A risk adjustment margin for the maximum amount the insurer rationally would pay to be relieved of the risk that the ultimate fulfillment cash flows exceed those expected (risk adjustment margin), which would be estimated using one of three techniques (confidence level, conditional tail expectation, or cost of capital) that are prescribed in the IASB's proposed standard (see paragraphs B73–B103 of the IASB's Exposure Draft).
c. A residual margin, which represents the excess of the expected present value of cash inflows over the expected present value of the cash outflows plus the risk adjustment margin.

53. The combination of items (a) and (b) in paragraph 52 represents the present value of the fulfillment cash flows[10] as described in paragraphs 17–22 of the IASB's Exposure Draft.

54. Under the Board's composite margin approach, an insurer would measure an insurance contract initially as the sum of the following:

a. The present value (unbiased and probability-weighted estimate) of the expected cash outflows less cash inflows that are expected to arise as the insurer fulfills the insurance contract
b. A composite margin that represents the excess of the expected present value of cash inflows over the expected present value of the cash outflows.

55. An insurer would determine the composite or residual margin at a level that aggregates insurance contracts into a portfolio of insurance contracts and within a portfolio, by similar date of initial recognition of the contract and coverage periods.[11]

Cash Flows

56. Estimates of cash flows (other than acquisition costs—see paragraphs 59 and 60) would include only cash flows within the boundary of an existing contract that are incremental at the level of a portfolio of insurance contracts. Those incremental cash outflows would include direct costs and systematic allocations of costs that relate directly to the insurance contracts or contract activities.

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[10]The IASB's Exposure Draft defines *present value of the fulfillment cash flows* as the expected present value of the future cash outflows less future cash inflows that will arise as the insurer fulfills the insurance contract, adjusted for the effects of uncertainty about the amount and timing of those future cash flows.

[11]A portfolio of insurance contracts would be made up of insurance contracts that are subject to broadly similar risks and managed together as a single pool.

57. Estimates of cash flows (other than acquisition costs) for a portfolio of insurance contracts would include all incremental cash inflows and cash outflows arising from that portfolio and would:

a. Be explicit (that is, distinct from estimates of discount rates that adjust those cash flows for the time value of money and, for the two-margin approach only, the risk adjustment margin that reflects the effects of uncertainties in the amount and timing of those cash flows)
b. Reflect the perspective of the entity but, for market variables, be consistent with observable market inputs
c. Incorporate all available information about the amount, timing, and uncertainty of net cash flows that will arise as the insurer fulfills the insurance contract
d. Reflect all available information at the measurement date
e. Include only those net cash flows that arise from existing contracts (that is, cash inflows and outflows that arise within the boundary of those contracts).

58. The estimates of net cash flows from a portfolio of insurance contracts would equal the sum of the estimated net cash flows of the individual contracts. Therefore, the level of aggregation for measurement would not affect the present value of the probability-weighted estimate of the net cash flows.

Acquisition costs

59. *Acquisition costs* would be defined as the direct and indirect costs of selling, underwriting, and initiating an insurance contract. However, acquisition costs would be included in the cash outflows used to measure an insurance liability only if those costs are *incremental* (that is, those costs that would not have been incurred if the insurer had not issued that particular contract). Those costs would be identified at the level of an individual insurance contract rather than at the level of a portfolio of insurance contracts. Acquisition costs that are not identified as incremental at initial recognition of an insurance contract would be expensed as incurred.

60. Acquisition costs included in the present value of the probability-weighted estimate of net cash flows would reduce the residual (or composite) margin at initial recognition of the contract. Thus, acquisition costs would affect profit over the coverage and claims handling periods (or solely over the coverage period under the two-margin approach). Accordingly, acquisition costs would not be explicitly amortized.

61. The types of acquisition costs that would be included in measurement of the insurance liability under the building-block approach likely would differ from the types of costs that would be deferred under the final consensus reached in EITF Issue No. 09-G, "Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts." If affirmed by the Board, Issue 09-G would further align the requirements to capitalize acquisition costs by insurance entities

with the requirements to capitalize loan origination costs in Subtopic 310-20. Specifically, only the following costs incurred in the acquisition of new and renewal insurance contracts would be capitalized as deferred acquisition costs under Issue 09-G:

a. Incremental direct costs of a successful contract acquisition
b. The portion of the insurance entity employee's total compensation and payroll-related fringe benefits directly related to time spent performing acquisition activities for a contract that has actually been acquired.

62. Issue 09-G also specifies that advertising costs would be capitalized only if the criteria in items (a) and (b) of the previous paragraph are met for capitalizing such costs pursuant to the direct response advertising guidance in Topic 340, Other Assets and Deferred Costs. Additionally, Issue 09-G specifies that if those criteria are met, the direct-response advertising costs would be included in deferred acquisition costs for classification, subsequent measurement, and premium deficiency purposes.

63. Issue 09-G is expected to be published as a final Accounting Standards Update in the fourth quarter of 2010.

Time value of money

64. The carrying amount of an insurance liability would include the present value of the probability-weighted estimate of net cash flows at the end of each reporting period using discount rates that:

a. Are consistent with observable current market prices for instruments with cash flows whose characteristics reflect those of the insurance contract liability (that is, in terms of timing, currency, and liquidity)
b. Exclude any factors that influence the observed rates but are not relevant to the insurance contract liability (for example, risks that are not present in the liability but are present in the instrument for which the market prices are observed).

65. As a result of the conditions in paragraph 64, if the cash flows of an insurance contract do not depend on the performance of specific assets, the discount rate would reflect the yield curve in the appropriate currency for instruments that expose the holder to no credit risk or negligible credit risk, with an adjustment for illiquidity. Thus, in estimating discount rates for an insurance contract, an insurer would consider any differences between the liquidity characteristics of the instruments underlying the rates observed in the market and the liquidity characteristics of the insurance contract.

Two-Margin Approach

66. The risk adjustment margin in the two-margin approach is intended to represent the maximum amount that the insurer rationally would pay to be relieved of the risk that the ultimate fulfillment cash flows exceed those expected. An insurer would estimate the risk adjustment margin at the level of a portfolio of insurance contracts. Therefore, the risk adjustment margin would reflect the effects of diversification that arise within a portfolio of insurance contracts but not the effects of diversification between that portfolio and other portfolios of insurance contracts.

67. The benefits of a two-margin approach include the following:

   a. A risk adjustment margin would depict an explicit assessment of the maximum amount an insurer rationally would pay to be relieved of the risk that the ultimate fulfillment cash flows exceed those expected, which some have said would reflect the uncertainty in possible outcomes.
   b. After initial recognition, a risk adjustment margin would be remeasured each reporting period and, accordingly, would reflect changes in the maximum amount an insurer rationally would pay to be relieved of the risk that the ultimate fulfillment cash flows exceed those expected. The period-to-period changes in the risk adjustment margin would be recognized in earnings over the coverage and claims handling periods.
   c. The residual margin would be recognized subsequently in earnings over the coverage period only, because the residual margin is not designed to capture risk. The residual margin would be recognized in a systematic manner on the basis of the passage of time unless the pattern of expected claims and benefits indicates that another pattern would be more appropriate.

68. Some have said that the resulting recognition of the risk adjustment margin over the coverage and claims handling periods properly reflects the economic drivers of the contract and any resulting changes. Others noted that the measurement of the risk adjustment margin would be too subjective and would result in additional costs without a sufficient increase in decision usefulness or reliability. Additionally, opponents note that the two-margin approach is more likely to generate a loss at initial recognition than the composite margin approach and, therefore, does not faithfully represent the economics of the insurance contract (see the examples in paragraph 72).

Composite Margin Approach

69. Risk associated with the uncertainty in net cash flows of an insurance contract would be considered in that contract's pricing and, therefore, would be implicit in the composite margin. The composite margin also would implicitly include the potential profit on the contract, measured as the difference between the present value of expected premiums and benefits, claims, and expenses.

70. Proponents of a composite margin approach would prefer not to use an explicit risk adjustment margin for the measurement of an insurance contract because of the level of judgment required in selecting a risk methodology and the lack of comparability that would result. If a risk adjustment margin is not explicitly determined upon initial recognition, risk and uncertainty would be reflected through a single composite margin.

71. The benefits of a composite margin approach include the following:

a. The approach would be more consistent with the allocated transaction price approach in the proposed Accounting Standards Update on revenue recognition, because both a composite margin and a residual margin are allocations of the customer consideration, whereas a risk adjustment margin would be subsequently remeasured.
b. A composite margin would eliminate the need to use subjective methods for measuring the risk adjustment margin that may decrease comparability. Furthermore, changes in those subjective measurements from period to period would be recognized immediately in earnings.
c. A composite margin would provide a simpler and more understandable approach to account for the difference between the expected cash inflows and outflows. The method for subsequent recognition of the composite margin in earnings would be simpler to calculate and more transparent to users of financial statements than the IASB's proposed techniques for subsequent recognition of changes in the risk adjustment margin.

Initial Measurement Examples

72. The following examples illustrate the application of the basic elements of the building-block approach using the two-margin and composite margin approaches. As noted in paragraph 68 and illustrated below in Example 2, the two-margin approach is more likely to generate a loss at initial recognition than the composite margin approach.

Example 1

An insurer issues an insurance contract, receives CU50 as the first premium payment, and incurs acquisition costs of CU70, of which incremental acquisition costs are CU40. The insurer estimates that the present value of the future premiums is CU950. Therefore, the present value of all premium payments is CU1,000. Additionally, the insurer estimates that the present value (unbiased and probability-weighted estimate) of the future claims is CU900.

Under the two-margin approach, the risk adjustment margin is estimated to be CU50 and, therefore, the residual margin is estimated to be CU10. Under the composite margin approach, the margin is CU60 (which is equal to the risk adjustment and residual margins under the two-margin approach). At initial recognition, the insurer would measure the insurance contract as follows:

	Two-Margin Approach	**Composite Margin Approach**
Present value of cash inflows (premiums)	1,000	1,000
Present value of cash outflows (claims and incremental acquisition costs)	(940)	(940)
Net present value of net cash flows	60	60
Composite margin	–	(60)
Risk adjustment margin	(50)	–
Residual margin	(10)	–
Insurance liability at initial recognition	–	–

Additionally, the nonincremental acquisition costs of CU30 (CU70 – CU40) would be immediately expensed at initial recognition under both approaches.

Example 2

Assume the same facts as in Example 1, except that the insurer estimates that the present value of the cash outflows is CU920. At initial recognition, the insurer would measure the insurance contract as follows:

	Two-Margin Approach	Composite Margin Approach
Present value of cash inflows (premiums)	1,000	1,000
Present value of cash outflows (claims and incremental acquisition costs)	(960)	(960)
Present value of net cash flows	40	(40)
Composite margin	–	40
Risk adjustment margin	(50)	–
Residual margin	–	–
Insurance liability at initial recognition (loss at initial recognition)	(10)	–

The nonincremental acquisition costs of CU30 (CU70 – CU40) would be immediately expensed at initial recognition under both approaches. Accordingly, the effect on earnings at initial recognition would be as follows:

	Two-Margin Approach	Composite Margin Approach
Contract loss at initial recognition	(10)	–
Non-incremental acquisition costs	(30)	(30)
Total loss at initial recognition	(40)	(30)

Under the composite margin approach, a contract loss would not be recognized at initial recognition. As explained in paragraphs 80–88, the composite margin of CU40 would be recognized in earnings over the coverage and claims handling periods.

However, under the two-margin approach, a contract loss of CU10 would be recognized at initial recognition and, as explained in paragraphs 75 and 76, the risk adjustment margin of CU50 would be subsequently remeasured each reporting period with changes recognized in earnings over the coverage and claims handling periods based on that remeasurement.

Questions for Respondents

7. Do you agree with the use of the probability-weighted estimate of net cash flows to measure insurance contracts? Does that approach faithfully represent the economics of insurance contracts? Is it an improvement over existing U.S. GAAP?

8. Do you think that an entity's estimate of the net cash flows should include a risk adjustment margin?

9. Is the objective of the risk adjustment margin understandable? If so, do you think that the techniques for estimating the risk adjustment margin (see paragraph 52(b)) faithfully represent the maximum amount that the insurer would rationally pay to be relieved of the risk that the ultimate fulfillment cash flows exceed those expected?

10. Do you think that the risk adjustment margin would be comparable for entities that are exposed to similar risks?

11. Do you agree with the description of cash flows that should be included in the measurement of an insurance contract? Is the proposed guidance operational?

12. Do you agree that the carrying amount of all insurance contracts should be discounted if the effect is material? Do you agree with the proposed guidance on the discount rate that should be used to measure the carrying amount of insurance contracts? If not, which discount rate should be used?

13. Do you think that acquisition costs should be included as one of the cash flows relating to the contract? If not, how would you account for acquisition costs?

14. Do you agree that acquisition costs included in the cash flows used in the measurement of the insurance contract should be limited to those that are incremental at the individual contract level? If not, which acquisition costs, if any, would you include in the measurement of the insurance contract?

Subsequent Measurement

73. An insurer would recognize the effects of changes in the present value of estimates of probability-weighted net cash flows immediately in earnings. Both approaches initially calibrate the residual margin and the composite margin to the consideration received or receivable from the policyholder. However, the following differences arise after initial recognition.

a. The residual margin in the two-margin approach would be recognized in earnings over the coverage period, while the composite margin would be recognized in earnings over both the coverage and claims handling periods.
b. The risk adjustment margin in the two-margin approach would be remeasured each reporting period during the coverage and claims handling periods. That remeasurement would reflect any changes in the maximum amount that the insurer would rationally pay to be relieved of the uncertainty that the ultimate fulfillment cash flows will exceed those expected.
c. Interest would be accreted on the residual margin under the two-margin approach. In contrast, interest would not be accreted on the composite margin under the composite margin approach.

Two-Margin Approach

74. The carrying amount of the insurance contract would be remeasured at the end of each reporting period as the sum of the present value of the fulfillment cash flows at that date (including the risk adjustment margin) and the remaining amount of the residual margin.

Risk Adjustment

75. As noted in paragraph 67(b), the risk adjustment margin would be remeasured at the end of each reporting period using one of the following techniques (see paragraphs B73–B90 of the IASB's Exposure Draft):

a. Confidence level
b. Conditional tail expectation
c. Cost of capital.

76. Changes in the risk adjustment margin would be subsequently recognized in earnings over the coverage and claims handling periods on the basis of those remeasurements.

Residual Margin

77. In the IASB's view, the factors implicitly included in the residual margin would no longer be relevant after the end of the coverage period. Therefore, the residual margin would be recognized in earnings over the coverage period in a systematic way that best reflects the exposure from providing insurance coverage, as follows:

a. On the basis of passage of time, but
b. On the basis of the expected timing of incurred claims and benefits, if that pattern differs significantly from the passage of time.

78. The residual margin determined at initial recognition of the contract would not be remeasured in subsequent periods as a result of changes in estimates of cash flows or risk. However, the amount recognized in earnings would reflect the remaining portion of the residual margin for any contracts that are no longer in force at the end of the reporting period.

79. Additionally, an insurer would accrete interest on the carrying amount of the residual margin using the same discount rate that was used to determine the present value of the fulfillment cash flows at the initial recognition of the insurance contract (see paragraphs 64 and 65).

Composite Margin Approach

80. The majority of the Board members prefer that the subsequent measurement of the carrying amount of the insurance contract include a current assessment of the present value of the probability-weighted estimate of net cash flows (that is, the amount would be remeasured at the end of each reporting period). Changes in estimates of the net expected cash flows would be recognized in earnings immediately.

81. One of the primary differences between the Board's composite margin approach and the IASB's two-margin approach is the pattern of recognition of the margins in earnings. In the IASB's two-margin approach, risk would be considered in the risk adjustment margin, which would be remeasured each period with changes recognized in earnings over the coverage and claims handling periods. Additionally, the residual margin would be recognized in earnings solely over the coverage period.

82. In the Board's approach, an insurer's exposure to risk would be embedded in the composite margin. Thus, the composite margin would be recognized in earnings over the coverage and claims-handling periods to reflect the insurer's exposure to uncertainties related to the amount and timing of net cash flows.

83. To reflect the uncertainties about the amount and timing of expected net cash flows, the composite margin would be recognized in earnings over the coverage and claims handling periods using the following ratio:[12]

$$\frac{\text{(Premiums allocated to date + Claims and benefits paid to date)}}{\text{(Total expected premiums + Total expected claims and benefits)}}$$

84. An insurer would apply the ratio to the composite margin determined at initial recognition of the insurance contract. The resulting amount less the composite margin recognized in earnings in previous periods would be recognized in current period earnings.

85. The total expected premiums would be allocated over the coverage period in a systematic manner on the basis of the passage of time unless the pattern of expected claims and benefits indicates that another allocation would be more appropriate to best reflect the exposure from providing insurance coverage.

86. As evidenced by the ratio, the premiums allocated to date and the claims and benefits paid to date would be compared with the total expected premiums and the total expected claims and benefits. Each of the components that are included in the ratio (both in the numerator and in the denominator) would be updated each reporting period to reflect changes in the total expected premiums and the total expected claims and benefits over the coverage and claims handling periods. Thus, the composite margin recognized in earnings each period would be based on a ratio that reflects current estimates and experience under the contract.

87. The portion of the composite margin recognized in the current period would be based on the protection component (premium) of the contract and the insurer's exposure to risk from uncertainties related to cash flows that may arise from claims and benefits. The ratio likely would result in a greater amount of the composite margin recognized during the coverage period to reflect the insurer's exposure to risk during that period. An example demonstrating the method in which the composite margin would be recognized in earnings is presented in paragraph 89.

88. Similar to the subsequent measurement of the residual margin in the IASB's two-margin approach, the composite margin amount measured at initial recognition, to which the ratio would be applied each period, would not be remeasured in subsequent reporting periods for changes in cash flow estimates. Although the composite margin would not be remeasured in subsequent periods,

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[12]The ratio is described as the following formula in the appendix to the Basis for Conclusions of the IASB's Exposure Draft:

$$\frac{\text{(Premium allocated to current period + Current period claims and benefits)}}{\text{(Total contract premium + Total claims and benefits)}}$$

To better clarify the manner in which the composite margin would be recognized in earnings, the components of the ratio have been revised as described above.

the portion of the composite margin recognized in earnings would vary over the coverage and claims handling periods because the ratio would be updated each period for actual claims and benefits paid during the period and changes in expected cash flows. However, in contrast to the residual margin in the IASB's approach, the composite margin in the Board's approach would not accrete interest (see paragraphs 90–92).

Composite Margin Subsequent Recognition Example

89. The following example illustrates the subsequent recognition of the composite margin in earnings over the coverage and claims-handling periods. The example has significant simplifications, and rounding differences may exist.

Example 3

Assume the following:

a. Twenty policies with contract premiums of CU1,000 are paid at the beginning of each year for 3 years. Thus, the total expected premiums over the life of the contracts are CU60,000. The insurer will provide coverage for a period of 3 years and expects claims and benefits to be paid over a period of 5 years. Incremental acquisition costs of CU100 are incurred for each contract at the beginning of the first year. Thus, total incremental acquisition costs are CU2,000.
b. At initial recognition of the contracts (January 1, 20X1), the insurer expects to pay total claims and benefits of CU48,000. At the end of each year, the insurer updates this estimate as follows:
    1. 20X1: CU43,500
    2. 20X2: CU40,500
    3. 20X3: CU43,000
    4. 20X4: CU46,500
    5. 20X5: CU45,000.
c. The composite margin determined at initial recognition is CU13,272, which is measured as the difference between the present value of the expected premiums and the present value of the expected claims, benefits, and expenses.
d. Subsequently, the insurer pays claims and benefits as follows:
    1. 20X1: CU6,000
    2. 20X2: CU7,000
    3. 20X3: CU15,000
    4. 20X4: CU11,000
    5. 20X5: CU6,000.

The ratio used to recognize composite margin in earnings is as follows:

$$\frac{\text{(Premiums allocated to date + Claims and benefits paid to date)}}{\text{(Total expected premiums + Total expected claims and benefits)}}$$

Based on the assumptions and the ratio, the insurer recognizes the composite margin as follows:

	20X1	20X2	20X3	20X4	20X5
Premiums allocated to the current period	20,000	20,000	20,000	-	-
Premiums allocated to date	20,000	40,000	60,000	60,000	60,000
Total expected premiums	60,000	60,000	60,000	60,000	60,000
Current period claims and benefits payments	6,000	7,000	15,000	11,000	6,000
Claims and benefits paid to date	6,000	13,000	28,000	39,000	45,000
Total expected claims and benefits	43,500	40,500	43,000	46,500	45,000
Ratio calculated for the period	0.2512	0.5274	0.8544	0.9296	1.0000
Composite margin recognized in earnings to date	3,334	6,999	11,339	12,338	13,272
Less: composite margin recognized in previous periods	-	3,334	6,999	11,339	12,338
Composite margin recognized in current period	**3,334**	**3,665**	**4,340**	**998**	**935**
Remaining composite margin	9,938	6,273	1,938	935	-

Accretion of Interest on the Margins

90. The IASB's Exposure Draft proposes the residual margin accrete interest for the following reasons:

a. At initial recognition, the residual margin can be viewed as an allocation of part of the transaction price—that is, consideration paid or payable by the policyholder. The accretion of interest reflects that the entity rationally would have charged a different amount if the contract had stipulated earlier or later payments from the policyholder. Thus, accretion of interest shows the effect of the financing separately from the revenue from goods or services.
b. The residual margin is one part of an overall measure of the insurance contract, and every other component of that measure reflects the time value of money, which results in the subsequent accretion of interest.

91. Because the residual margin would be determined at initial recognition, and would not be remeasured thereafter, the interest rate used to accrete interest on the residual margin would be locked in upon initial recognition of the insurance contract. Furthermore, the rate would be the same interest rate as that used to discount cash flows included in the initial measurement of the liability (see paragraphs 64 and 65).

92. In contrast to the IASB's proposal, the Board's preliminary view is that interest would not be accreted on the composite margin. The majority of Board

members have said that interest expense should not be recognized because it will increase the composite margin and result in additional revenue recognized. Some Board members also do not believe that interest expense should be recognized because they view the composite margin as a noncash item that eliminates day one gains, rather than as an obligation (that is, expected future net cash flows). Therefore, a majority of the Board members noted that accretion of interest on the composite margin would not be appropriate.

Derecognition

93. An insurer would remove an insurance liability (or part of an insurance liability) from its statement of financial position only when it is extinguished (that is, when the obligation specified in the insurance contract is discharged, cancelled, or expired). At that point, the insurer would not be at risk and, therefore, would not be required to transfer any further economic resources to satisfy the insurance contract.

Questions for Respondents

15. Do you agree with the use of either the composite margin approach or two-margin approach to measure the net insurance contract? Does either approach faithfully represent the economics of insurance contracts? Is either approach an improvement over the measurement used in current U.S. GAAP?

16. Do you think that the composite margin should be recognized in earnings in subsequent periods using the ratio described in paragraph 83? If not, how would you recognize the composite margin in earnings?

17. Do you agree that interest should not be accreted on the composite margin? Why or why not?

Two Accounting Approaches for Insurance Contracts

94. In addition to the building-block approaches discussed above, the Boards are considering a modified approach for the preclaims liability of certain insurance contracts. Similar to current guidance on short-duration contracts in Topic 944, the proposed modified approach would measure a preclaims liability (that is, the performance obligation) using an unearned premium approach that is consistent with the customer consideration approach in the proposed Accounting Standards Update on revenue recognition. As the insurer fulfills the performance obligation to provide insurance coverage continuously over the coverage period, the insurer would be released from risk and the related part of the premium (that is, the preclaims liability) would be considered earned and therefore, would be recognized as revenue in the current period.

95. The modified approach was initially developed to provide a more meaningful presentation of the insurance liability and the related revenues and expenses for certain contracts that do not contain significant embedded derivatives for the following reasons:

a. The unearned premium is a reasonable approximation of the claims liability, measured as the present value of the probability-weighted estimate of net cash flows, plus profit on those (for the IASB, the present value of the fulfillment cash flows, plus profit on them).
b. Current practice for the preclaims liability for nonlife insurance contracts is based on such an approach.

IASB's Modified Approach for Certain Contracts (Typically Short Duration)

Scope

96. The IASB proposes that a modified approach should be required for short-duration contracts that meet both of the following conditions:

a. The coverage period of the insurance contract is approximately one year or less.
b. The contract does not contain embedded options or other derivatives that significantly affect the variability of cash flows, after unbundling any embedded derivatives.

Recognition and Initial Measurement

97. Under the modified approach, the IASB's Exposure Draft distinguishes between a *preclaims liability* and a *preclaims obligation*. The IASB's Exposure Draft defines the *preclaims liability* as an insurer's stand-ready obligation to pay valid claims for future insured events arising under existing contracts. The preclaims liability is the preclaims obligation less the expected present value of future premiums, if any, that are within the boundary of the existing contract. The preclaims obligation is measured at initial recognition as the premium, if any, received at initial recognition, plus the expected present value of future premiums, if any, that are within the boundary of the existing contract less the incremental acquisition costs. Thus, the preclaims liability at initial recognition is equal to the premiums received, if any, at initial recognition less the incremental acquisition costs.

98. An insurer would recognize a preclaims liability at initial recognition for a short-duration insurance contract. The primary differences regarding the recognition of the insurance contract under the modified approach are that the measurement of the preclaims liability during the preclaims period does not explicitly include the components of the building-block approach, and that changes would be presented in the statement of comprehensive income, as

explained in paragraph 104. However, to be consistent with the two-margin approach, the modified approach proposed by the IASB also would include the following features:

a. Interest would be accreted on the carrying amount of the insurance contract if the effect of the time value of money is material.
b. The basis for the onerous contract test would be the present value of the fulfillment cash flows (as measured under in the IASB's two-margin approach). Considering the short duration of the coverage period, the level of aggregation for the onerous contract test would be within the portfolio of insurance contracts by similar date of initial recognition.
c. The incremental acquisition costs would not be presented as an asset but, rather, as a reduction of the unearned premiums (preclaims liability).

Subsequent Measurement

99. In paragraph BC146 of the IASB's Exposure Draft, the IASB states that if significant changes in estimates are made during the coverage period of a short-duration contract, those changes are more likely to be unfavorable (that is, leading to losses) than favorable (that is, leading to gains). As a result, the insurer would recognize those losses when the contract becomes onerous. In the IASB's view, for contracts meeting the conditions listed in paragraph 96, the unearned premium would be a reasonable approximation of the present value of the fulfillment cash flows plus the residual margin (and would achieve a similar result at a lower cost).

100. The preclaims obligation (plus incremental acquisition costs) would be recognized as revenue in earnings over the coverage period in a systematic way that best reflects the exposure from providing insurance coverage (usually, straight line). Although incremental acquisition costs initially would be recognized as a reduction of the preclaims liability, the incremental acquisition costs subsequently would be recognized as an expense in a pattern similar to that used for amortizing the premiums.

101. The remaining unearned premiums (less unamortized incremental acquisition costs) would be the preclaims liability for unexpired contract terms. Interest would be accreted on the carrying amount of the preclaims liability using the current discount rate. The use of the current discount rate is different from the discount rate used to accrete interest on the residual margin (that is, the accretion rate applied to the residual margin would be locked in upon initial recognition of the contract).

102. As insured events occur, an insurer would separately recognize a claims liability.[13] That liability would be measured as the probability-weighted estimate of the net cash flows (for the IASB, the present value of the fulfillment cash flows) under the building-block approach at the end of each reporting period. The liability would include claims incurred whether or not reported to the insurer.

103. An insurance contract would be onerous if the present value of the fulfillment cash flows (as measured under the two-margin approach) relating to future insured claims exceeds the carrying amount of the preclaims obligation. Thus, an insurer would calculate the present value of the fulfillment cash flows regardless of whether the contract is short duration or long duration, which would diminish the benefits of the modified approach for short-duration contracts that require application of the onerous test.

Presentation

104. Under the IASB's proposal, preclaims liabilities measured under the modified approach would not be presented in the statement of comprehensive income as changes in a single contract liability (see paragraphs 122–124). Instead, an insurer would separately present premium revenue (determined as the gross amount of the preclaims obligation earned in the current period), claims and expenses incurred, and the amortization of incremental acquisition costs included in the preclaims obligations. Although the amount of the preclaims obligation earned in the current period would be presented gross in the statement of comprehensive income, the preclaims liability would be presented as a single net liability on the statement of financial position. Thus, the preclaims liability in the statement of financial position would be presented similarly to the insurance liability measured under the building-block approach.

FASB's Preliminary Views

105. Several Board members expressed a preliminary view that a modified approach would be applied to some insurance contracts (for example, certain short-duration contracts). The Board has not determined the extent to or the conditions under which a modified approach would apply. Current guidance requires that insurance contracts be classified as short duration or long duration depending on whether the contracts are expected to remain in force for an extended period. The period of short duration is not explicitly defined, but in practice is generally one year or less. The Board is considering whether current guidance is appropriate for determining the insurance contracts to which a modified approach would apply or whether stakeholders recommend any improvements.

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[13]The IASB's Exposure Draft defines *claims liability* as the liability to pay valid claims for insured events that have already occurred, including claims incurred but not reported.

106. Although several Board members agree with some of the recognition and measurement provisions for the modified approach in the IASB's Exposure Draft, the Board has not determined the following:

a. Whether incremental acquisition costs would reduce the preclaims liability
b. Whether interest would be accreted on the carrying amount of the preclaims liability
c. How the onerous test would be applied to the preclaims liability
d. How insurance contracts would be presented in the financial statements.

107. The Board requests input from stakeholders on whether a different approach should continue to be used for some insurance contracts and, if so, what criteria should be used to distinguish those contracts (for example, type or duration of contract) and how that approach should be applied.

Questions for Respondents

18. Do you think that all insurance contracts should be recognized and measured using one approach or that certain insurance contracts should be recognized and measured using an alternative approach (for example, the modified approach)? Why or why not?
19. If an alternate approach is required for some insurance contracts, what recognition, measurement, and presentation provisions should be applied (including those items noted in paragraph 106)?
20. Do both the building-block approach and the modified approach (with the latter approach applied only to certain short-duration contracts) produce relevant and decision-useful information? Why or why not?
21. How should the scope of insurance products for each approach be defined (for example, duration of coverage period, duration of claims payment period, or type of insurance)?
22. Are there specific types of insurance contracts for which the approaches would not provide decision-useful information?
23. What are the implications of the recent U.S. healthcare reform to the application of the proposed contract boundary principle, including whether health insurance contracts written under the new reforms would meet the conditions in the proposed guidance to be accounted for under the modified approach?
24. What other changes should be considered to both improve and simplify U.S. GAAP for short- and long-duration insurance contracts?
25. What are the incremental costs of adopting the alternatives described in this Discussion Paper? Please separately describe one-time costs and ongoing costs.

REINSURANCE

108. A reinsurance contract is an insurance contract issued by one insurer (the reinsurer)[14] to compensate another insurer (the cedant)[15] for losses on one or more contracts issued by the cedant. A reinsurer would use the same recognition and measurement approach for reinsurance contracts as that used for direct insurance contracts.

109. A cedant would not offset reinsurance assets[16] against related insurance liabilities because the liability would not be extinguished, and typically there would be no legal right of offset. However, those reinsurance assets would be measured using the same basis as the underlying insurance liability, which would include the following:

a. The present value of the probability-weighted estimate of net cash inflows from the reinsurer less the present value of the cedant's expected payments to the reinsurer (for the IASB, the expected present value of the fulfillment cash flows)
b. A composite margin (for the IASB, a residual margin) to eliminate any loss at initial recognition of the reinsurance contract.

110. The cedant would estimate the present value of the net cash flows in the same manner as the corresponding part for the present value of the future net cash flows for the underlying insurance contract. If the future cash inflows exceed the future cash outflows, a gain would be recognized in earnings. However, if the future cash inflows are less than the future cash outflows, the difference would be recognized in the composite margin (for the IASB, the residual margin).

111. An example illustrating the application of those principles is included in paragraph B36 of the IASB's Exposure Draft.

Questions for Respondents

26. The scope of the proposed guidance includes reinsurance contracts that an insurer issues or acquires. However, insurance contracts held directly by other policyholders would be excluded from the scope of the proposed guidance. Do you agree with this exclusion? Why or why not?

27. Should there be symmetry between the recognition and measurement of reinsurance contracts and the underlying contract ceded?

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[14]A *reinsurer* would be defined as the party that has an obligation under a reinsurance contract to compensate a cedant if an insured event occurs.
[15]A *cedant* would be defined as the policyholder under a reinsurance contract.
[16]A *reinsurance asset (or liability)* would be defined as a cedant's net contractual rights (or obligations) under a reinsurance contract.

PRESENTATION AND DISCLOSURE

Presentation

Statement of Financial Position

112. The presentation of the combination of rights and obligations arising from an insurance contract as a single net liability (or a single net asset) would be consistent with the measurement of an insurance contract asset or liability based on net cash flows. Therefore, the IASB proposes that an insurer present each portfolio of insurance contracts as a single item within insurance contract assets or insurance contract liabilities.

113. Specific guidance and further detail on the proposed presentation requirements for the statement of financial position are contained in paragraphs 69–71 of the IASB's Exposure Draft.

Statement of Comprehensive Income

114. The Boards considered several approaches for presenting income and expenses arising from insurance contracts: a margin presentation approach and two different premium presentation approaches. The following section discusses those approaches. Additional information about those approaches is included in paragraphs BC159–BC170 of the IASB's Exposure Draft.

Margin Presentation Approach

115. Revenues and claims and benefits expenses would not be presented separately. Instead, earnings would present changes in the margins determined at initial recognition of the insurance contracts (the composite margin under the Board's preliminary views or the residual and risk adjustment margins under the IASB's proposals). Subsequent experience adjustments and changes in estimates of expected cash flows also would be presented separately.

Advantages and disadvantages of the margin presentation approach

116. Proponents of the margin presentation approach have said that it has the following advantages:

a. It links the presentation approach in the statement of comprehensive income to the measurement approach for the insurance liability.
b. Deposit receipts would not need to be unbundled from the premiums because premiums would be treated the same as deposits. Distinguishing between the deposits and the premiums may be somewhat arbitrary for some contracts.

117. Opponents of the margin presentation approach have said that it has the following disadvantages:

a. Because the amount of premiums and claims related to coverage provided by an insurer during the period would not be presented as revenue and expenses in the statement of comprehensive income, some elements of profitability, risk, and loss experience would be obscured. For example, if the contract transfers insurance risk, it would be inappropriate to present each arrangement as a deposit because:
    1. Premiums are not refunded if an insured event does not occur.
    2. The liability could far exceed the premiums if an insured event does occur.
b. Only part of the premium received from the policyholder is depicted as income—namely the composite margin (under the composite margin approach) or the risk adjustment and residual margins (under the two-margin approach). Income presented in the statement of comprehensive income would not be comparable with presentation approaches for revenue from other activities, such as fund management.

Premium Presentation Approaches

118. The Boards also considered the following two premium presentation approaches for revenues and expenses in the statement of comprehensive income:

a. Written premium presentation approach—Premiums would be presented as revenue when receivable. The corresponding increase in the liability would be presented as an expense when incurred. Many existing accounting models apply this approach to life insurance contracts.
b. Allocated premium presentation approach—Premiums received would be presented as preclaims liabilities in the statement of financial position (that is, as performance obligations). As the insurer performs under the contract by providing insurance coverage, the preclaims liability would be recognized in the statement of comprehensive income as premium revenue. Claims liabilities would be recognized as expenses when incurred. Many existing accounting models apply this approach to nonlife insurance contracts.

119. Under both of the premium presentation approaches, a true-up amount would be necessary for insurance contracts measured using the building-block approach. That amount would be equal to the difference between premium revenue and the claims and benefits expenses recognized in the statement of comprehensive income and would reconcile the difference between:

a. Premium revenue and claims and benefits expenses presented in the statement of comprehensive income, and
b. The amount of the composite margin recognized in current period earnings (for the two-margin approach, the residual margin and changes in the risk adjustment margin).

Advantages and disadvantages of a premium presentation approach

120. Supporters of a premium presentation approach note the following:

a. It would provide information about the amount of premiums relating to coverage provided during a period. Many users of financial statements regard such information as an important performance measure for an insurer.
b. Reported revenue would correspond with the customer consideration received for the premiums, which is consistent with the proposed Accounting Standards Update on revenue recognition.
c. It would provide information about claims expenses during the period including claims incurred but not reported and changes in the insurance liability.

121. Opponents of a premium presentation approach note the following:

a. The pattern of premium payments may not reflect the services provided by the insurer during the contract term because of the deposit element inherent in certain contracts. Therefore, a premium approach would be inconsistent with existing practices for recognizing and presenting revenue for noninsurance contracts.
b. Allocation of the premium or a part of that premium would be inherently difficult for some types of insurance contracts (for example, immediate annuities, stop-loss contracts, and contracts that contain significant guarantees and options).
c. A premium approach would not reflect changes in the individual components of the building blocks that are included in the measurement of an insurance contract.

IASB's Exposure Draft

122. The IASB proposes a presentation model for insurance contracts measured using the building-block approach based on the margin presentation approach. That presentation model would be consistent with the building-block approach because the line items presented would represent the changes in the individual building blocks. Specifically, the statement of comprehensive income would provide separate information about the following:

a. The change in the risk adjustment margin
b. The recognition of the residual margin in earnings (or the composite margin for the approach preferred by the Board)

c. The difference between the actual cash flows for the current period and previous estimates of those cash flows (that is, an experience adjustment)
d. Changes in estimates of future cash flows (remeasurements) during the period
e. Accretion of interest on insurance liabilities (presented or disclosed in a way that highlights the relationship between interest expense, changes in discount rates, and investment return on the assets that back those liabilities).

123. Although a margin presentation approach for the statement of comprehensive income would be required, information about total premiums, total claims, and administrative and acquisition expenses would be disclosed in the notes to the financial statements. The IASB proposes a different approach—the allocated premium presentation approach—for contracts accounted for under the modified approach (see paragraph 104). In the IASB's view, presenting the allocated premium (earned premium) as revenue and incurred claims as expenses for contracts accounted for under the modified approach would more faithfully represent those contracts.

124. For specific guidance and further detail on the proposed presentation requirements for the statement of comprehensive income, see paragraphs 72–78 of the IASB's Exposure Draft.

FASB's Preliminary Views

125. The majority of Board members agree with the IASB's proposal to use a margin presentation for insurance contracts measured under the building-block approach. Additionally, the Board has indicated a preference for the use of a premium presentation for contracts measured under the modified approach. However, the Board has not determined which contracts would be measured according to the modified approach and is concerned about the use of two different presentation approaches for insurance contracts. As such, the Board is soliciting additional feedback from stakeholders on the usefulness of the information provided by either a margin presentation approach or a premium presentation approach for insurance contracts and which contracts would use each approach.

Presentation Example

126. The following example illustrates the margin and premium presentation approaches under the two-margin approach and the composite margin approach. The example has significant simplifications, and rounding differences may exist. Furthermore, the example assumes that the effect of mortality experience on the total amount of the maturity benefits is not material.

Example 4

Assume the following:

a. One thousand policies with a premium of CU1,200 paid January 1, 20X1, provide coverage for any deaths occurring between January 1, 20X1, and December 31, 20X3. If the policyholders are alive on December 31, 20X3, a maturity benefit is paid. (All numbers below are presented in CU1,000.)
b. At initial recognition, the expected claims (including claims handling costs) are CU1,000.
    1. Death benefits: expected value of CU200, to be paid on December 31 each year
    2. Maturity benefits: expected value of CU400, to be paid on December 31, 20X3.
c. Other general and administrative expenses (nonincremental) are CU120, which are incurred evenly over the contract period and are not included in the measurement of the insurance contract.
d. At initial recognition, the expected investment return is 8 percent and the risk-free rate (adjusted for illiquidity) used to discount the expected cash flows is 5 percent.
e. Acquisition costs incurred at initial recognition of the contract are CU30.
    1. Incremental acquisition costs are CU10.
    2. Nonincremental acquisition costs are CU20.
f. On January 1, 20X1, the present value of the expected cash outflows (including expected death maturity benefits and incremental acquisition costs) is approximately CU900.
g. An insurer using the two-margin approach determines the risk adjustment margin to be CU200 and the residual margin to be CU100. The insurer expects to be released from all risk by the end of the coverage period.
h. The composite margin is CU300 (the difference between the premiums and the present value of the expected cash outflows) for an insurer using the composite margin approach.
i. At December 31, 20X1:
    1. The actual death benefits for the 12 months to that date are CU210.
    2. The insurer estimates that the expected claims for each of the remaining 2 years will increase from the original estimate of CU200 to CU215.
    3. The insurer using the two-margin approach remeasures the risk adjustment margin as CU160.
j. At December 31, 20X2:
    1. The actual death benefits for the 12 months to that date are CU220.
    2. The insurer estimates that the expected claims for the remaining year will increase from the estimate at December 31, 20X1, of CU215 to CU230.
    3. The insurer using the two-margin approach remeasures the risk adjustment margin as CU110.
k. At December 31, 20X3:
    1. The actual death benefits for the 12 months to that date are CU225.
    2. The insurer does not expect any cash flows beyond the end of the coverage period.
l. There are no differences between actual outcomes and previous estimates for all other assumptions.

Accordingly, the initial measurement of the insurance contract is as follows:

	Two-Margin Approach	Composite Margin Approach
Present value of cash inflows (premiums)	1,200	1,200
Present value of cash outflows (claims and incremental acquisition costs)	(900)	(900)
Present value of net cash flows	300	300
Composite margin	–	(300)
Risk adjustment margin	(200)	–
Residual margin	(100)	–
Insurance liability at initial recognition	–	–

The rollforward of the insurance liability for each year is as follows:

	Two-Margin Approach			Composite Margin Approach		
	20X1	20X2	20X3	20X1	20X2	20X3
Beginning liability balance	-	994	749	-	1,002	779
Premiums received	1,200			1,200		
Claims and benefits paid	(210)	(220)	(625)	(210)	(220)	(625)
Incremental acquisition costs	(10)			(10)		
Changes in the risk adjustment margin	(40)	(50)	(110)	-	-	-
Recognition of the residual margin[(a)]	(33)	(36)	(41)	-	-	-
Recognition of the composite margin[(b)]	-	-	-	(60)	(60)	(179)
Interest accreted on the expected net cash flows[(c)]	45	38	30	45	38	30
Interest accreted on the residual margin[(d)]	5	4	2	-	-	-
Experience adjustment[(e)]	10	5	(5)	10	5	(5)
Change in estimates[(f)]	28	14		28	14	
Total change in liability	994	(245)	(749)	1,002	(223)	(779)
Ending liability balance	994	749	-	1,002	779	-

(a) Recognized over the coverage period, with interest accreted on the carrying amount.
(b) Recognized according to the ratio and guidance in paragraphs 80–88.
(c) Interest is accreted on the present value of the net cash flows using the rate of 5 percent noted in the assumptions. For simplicity, 5 percent is used throughout the example but this rate is not locked in and may be changed over the coverage and claims handling periods.
(d) Interest is accreted on the carrying amount using the rate of 5 percent noted in the assumptions. The accretion rate for the residual margin is locked in at initial recognition of the contract.
(e) The difference between the actual and expected claims and benefits paid during the current period.
(f) The present value of the changes in estimates of future cash flows.

The measurement of the net insurance liability is the same regardless of the presentation approach used. Thus, the statement of financial position below and the rollforward are applicable to the three alternative presentation approaches for the statement of comprehensive income.

Statement of Financial Position

	Two-Margin Approach				Composite Margin Approach			
	Jan 1, 20X1	**Dec 31, 20X1**	**Dec 31, 20X2**	**Dec 31, 20X3**	**Jan 1, 20X1**	**Dec 31, 20X1**	**Dec 31, 20X2**	**Dec 31, 20X3**
Cash	1,200	1,016	837	239	1,200	1,016	837	239
Net insurance liability	(1,200)	(994)	(749)	-	(1,200)	(1,002)	(779)	-
Equity	-	22	88	239	-	14	58	239

As indicated by the total change in equity as of December 31, 20X3, the same amount of income is ultimately reported under both the two-margin approach and the composite margin approach, but the amount recognized throughout the period of contract fulfillment differs. Regardless of the presentation approach used, incremental acquisition costs are included in the measurement of the expected cash flows and non-incremental acquisition costs are expensed in the period incurred; that is, at the initial recognition of the contract. The net income recognized for each particular period is the same under all three presentation alternatives within each of the Boards' respective approaches. The different presentation approaches for the statement of comprehensive income are as follows:

Alternative 1: Margin Presentation Approach

The margin presentation approach is the preferred approach of the IASB, as noted in paragraph 122. Under the margin presentation approach, premiums are treated as deposits while claims and claims handling expenses are treated as repayments of deposits.

Statement of Comprehensive Income

	Two-Margin Approach				Composite Margin Approach			
	20X1	**20X2**	**20X3**	**Total**	**20X1**	**20X2**	**20X3**	**Total**
Risk adjustment margin	40	50	110	200	-	-	-	-
Residual margin	33	36	41	110	-	-	-	-
Composite margin	-	-	-	-	60	60	179	300
Insurance underwriting margin	73	86	151	310	60	60	179	300
Investment income[(a)]	96	81	67	244	96	81	67	244
Experience adjustment	(10)	(5)	5	(10)	(10)	(5)	5	(10)
Change in estimates	(28)	(14)	-	(42)	(28)	(14)	-	(42)
Interest accreted on the expected net cash flows	(45)	(38)	(30)	(113)	(45)	(38)	(30)	(113)
Interest accreted on the residual margin	(5)	(4)	(2)	(11)	-	-	-	-
Non-incremental acquisition costs	(20)	-	-	(20)	(20)	-	-	(20)
Other expenses[(b)]	(40)	(40)	(40)	(120)	(40)	(40)	(40)	(120)
Profit	22	66	151	239	14	44	181	239

(a) Based on the investment rate of 8 percent noted in the assumptions.
(b) General and administrative expenses.

Alternative 2: Written Premium Presentation Approach

Under the written premium presentation approach, the entire premium is reported as revenue on receipt. The change in the insurance liability represents significant events from accruing the premiums received at initial recognition and recognizing the part of the liability that covers the maturity benefit at the end of the contract.

Statement of Comprehensive Income

	Two-Margin Approach				Composite Margin Approach			
	20X1	**20X2**	**20X3**	**Total**	**20X1**	**20X2**	**20X3**	**Total**
Premium revenue	1,200			1,200	1,200			1,200
Investment income[a]	96	81	67	244	96	81	67	244
Residual/composite margin	33	36	41	110	60	60	179	300
Total income	1,329	117	108	1,555	1,356	142	246	1,744
Claims and benefits expenses	(210)	(220)	(625)	(1,055)	(210)	(220)	(625)	(1,055)
Non-incremental acquisition costs	(20)			(20)	(20)			(20)
Interest expense[b]	(50)	(42)	(32)	(123)	(45)	(38)	(30)	(113)
Other changes in the insurance liability[c]	(988)	251	740	3	(1,028)	201	630	(197)
Other expenses[d]	(40)	(40)	(40)	(120)	(40)	(40)	(40)	(120)
Total expenses	(1,307)	(51)	43	(1,315)	(1,342)	(97)	(65)	(1,505)
Profit	22	66	151	239	14	44	181	239

(a) Based on the investment rate of 8 percent noted in the assumptions.
(b) Interest accreted on the expected net cash flows (and residual margin under the two-margin approach).
(c) Determined as the sum of the experience adjustment, the change in estimates of future cash flows, the change in the risk adjustment margin (for the two-margin approach), and the difference between the premiums received and the claims and benefits paid during the period. That difference is included because the presentation of premium revenue and claims and benefits expenses each period does not correspond with the net measurement of the liability under the building-block approach.
(d) General and administrative expenses.

Alternative 3: Allocated Premium Presentation Approach

Under the allocated premium presentation approach, the premium is recognized as revenue based on performance of the contract over the coverage period in a systematic manner that best reflects the exposure from providing insurance coverage. In order to present premium revenue and claims and benefits expenses separately in the statement of comprehensive income but also measure the liability on a net basis, an amount representing the difference between the premium revenue allocated to the current period and the actual claims and benefits expenses incurred must be recognized so that profit is not changed as a result of using the allocated premium presentation approach. In the statement of comprehensive income below, that difference is included in the change in the insurance liability.

Statement of Comprehensive Income

	Two-Margin Approach				Composite Margin Approach			
	20X1	**20X2**	**20X3**	**Total**	**20X1**	**20X2**	**20X3**	**Total**
Premium revenue[(a)]	240	240	720	1,200	240	240	720	1,200
Investment income[(b)]	96	81	67	244	96	81	67	244
Residual/composite margin	33	36	41	110	60	60	179	300
Total income	369	357	828	1,555	396	382	966	1,744
Claims and benefits expenses	(210)	(220)	(625)	(1,055)	(210)	(220)	(625)	(1,055)
Non-incremental acquisition costs	(20)	-	-	(20)	(20)	-	-	(20)
Interest expense[(c)]	(50)	(42)	(32)	(123)	(45)	(38)	(30)	(113)
Other changes in the insurance liability[(d)]	(28)	11	20	3	(68)	(39)	(90)	(197)
Other expenses[(e)]	(40)	(40)	(40)	(120)	(40)	(40)	(40)	(120)
Total expenses	(347)	(291)	(677)	(1,315)	(382)	(337)	(785)	(1,505)
Profit	22	66	151	239	14	44	181	239

(a) Allocated based on the expected timing of claims and benefits payments at initial recognition of the contracts.
(b) Based on the investment rate of 8 percent noted in the assumptions.
(c) Interest accreted on the expected net cash flows (and residual margin under the two-margin approach).
(d) Determined as the sum of the experience adjustment, the change in estimates of future cash flows, the change in the risk adjustment margin (for the two-margin approach), and the difference between the premiums received and the claims and benefits paid during the period. That difference is included because the presentation of premium revenue and claims and benefits expenses each period does not correspond with the net measurement of the liability under the building-block approach.
(e) General and administrative expenses.

Questions for Respondents

28. The margin presentation approach highlights the changes in the insurance liability, rather than the current approach in U.S. GAAP, which presents, among other items, premium revenues, benefits paid, operating costs, and changes in loss estimates. Would this change improve your understanding of the performance of an entity that provides insurance (for some types of insurance or for all)? Please explain.

29. Should insurance contracts measured under the building-block approach be presented using a margin presentation approach or a premium presentation approach that would require a true-up amount as described in paragraph 119 (for example, the written allocation presentation approach or the allocated premium presentation approach)?

30. Should short- and long-duration (or nonlife and life) contracts be presented in a similar manner even if such contracts are measured under different approaches?

Disclosure

127. An insurer would disclose information about the amounts recognized in its financial statements in sufficient detail to help financial statements users evaluate the timing, amount, and uncertainty of future cash flows arising from insurance contracts and include the following:

a. A reconciliation of the opening and closing aggregate contract balances
b. The methods and inputs used to develop the measurements.

128. An insurer would disclose quantitative and qualitative information about the amounts recognized in its financial statements arising from insurance contracts and the nature and extent of risks arising from those contracts.

129. For specific guidance and further detail on the proposed disclosure requirements, see paragraphs 79–97 of the IASB's Exposure Draft.

130. The majority of the Board tentatively agrees with the disclosure requirements proposed by the IASB.

Question for Respondents

31. Do you agree with the proposed disclosures in the IASB's Exposure Draft? Why or why not? If not, what would you recommend and why?

ADDITIONAL QUESTION FOR RESPONDENTS

131. The IASB's Exposure Draft contains proposed guidance about topics not discussed in this Discussion Paper (for example, insurance contracts acquired in either a portfolio transfer or a business combination). Additionally, the IASB's Exposure Draft proposes transition requirements for adoption of the proposed insurance guidance. However, the Board has not addressed those topics. Respondents are encouraged to comment on those topics as well as any additional issues included in the IASB's Exposure Draft.

132. In addition to the questions presented throughout this Discussion Paper, the Board also requests input considering the following question.

Question for Respondents

32. After considering your views on the specific issues contained in this Discussion Paper and the IASB's Exposure Draft, what do you think would represent the most appropriate improvement to U.S. GAAP?

    a. Pursue an approach based on the IASB's Exposure Draft?
    b. Pursue an approach based on the IASB's Exposure Draft with some changes? Please explain those changes.
    c. Pursue an approach based on the Board's preliminary views in this Discussion Paper?
    d. Pursue an approach based on the Board's preliminary views with some changes? Please explain those changes.
    e. Make targeted changes to address specific concerns about current U.S. GAAP (for example, items included in paragraph 7)? Please describe those changes.

APPENDIX: SUMMARY OF CURRENT U.S. GAAP, THE IASB'S EXPOSURE DRAFT, AND THE FASB'S PRELIMINARY VIEWS

133. The following chart compares main areas of current U.S. GAAP for insurance contracts, the IASB's proposed approach, and the FASB's preliminary views that differ from the proposed approach included in the IASB's Exposure Draft. The summary of current U.S. GAAP included in the following chart is neither authoritative nor a substitute for current guidance in the *FASB Accounting Standards Codification*™. The following chart also is not intended to provide a complete discussion of current U.S. GAAP in comparison to the IASB's proposed approach and the FASB's preliminary views. Rather, it is intended to outline only significant topics that are deemed relevant for the purposes of this Discussion Paper. Furthermore, the FASB's preliminary views represent the views of the majority of the Board on each issue and may not be commonly held by all members of the Board.

	Item	Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
		Definition and Scope		
1	Scope	Insurance contracts (and reinsurance contracts) written by insurance entities included in the scope of Topic 944 (substantially all insurance entities).	• Insurance contracts (including reinsurance contracts) that an entity issues and reinsurance contracts that it holds. • Financial instruments that an entity issues containing a discretionary participation feature.	Same as the IASB's Exposure Draft except the Board would exclude financial instruments with discretionary participation features. Those contracts would be included within the scope of the guidance on financial instruments.
2	Scope Exceptions	No explicit scope exceptions stated.	• Product warranties issued by a manufacturer, dealer, or retailer. • Employers' assets and liabilities under employee benefit plans and retirement benefit obligations reported by defined benefit retirement plans (selfinsurance). • Contractual rights or obligations, contingent on the future use of, or right to use, a nonfinancial item. • Residual value guarantees. • Fixed-fee service contracts. • Contingent consideration payable or receivable in a business combination. • Direct insurance contracts that the entity holds.	Same as the IASB's Exposure Draft, except for the following: • The IASB's Exposure Draft would exclude from its scope employee benefit plans within the scope of IAS 19, *Employee Benefits* (which would include, among other items, health insurance provided by an employer). However, the Board questions whether health insurance provided by an employer should be excluded from the scope of the proposed guidance for U.S. GAAP. • The Board also would exclude financial instruments that contain discretionary participation features from the scope of the proposed

Item		Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
				guidance.
3	Definition of *Insurance Contract*	The Master Glossary of the Accounting Standards Codification defines an *insurance contract* as a contract in which an insurance entity unconditionally undertakes a legal obligation to provide specified benefits to specific individuals in return for a fixed consideration or premium.	A contract under which one party (the insurer) accepts significant insurance risk from another party (the policyholder) by agreeing to compensate the policyholder if a specified uncertain future event (the insured event) adversely affects the policyholder.	Same as the IASB's Exposure Draft.
4	Definition of *Insurance Risk*	Insurance risk is the risk arising from uncertainties about both underwriting risk and timing risk. Actual or imputed investment returns are not an element of insurance risk. Insurance risk is fortuitous; the possibility of adverse events occurring is outside the control of the insured.	Insurance risk is risk, other than financial risk, transferred from the holder of a contract to the issuer. A contract does not transfer insurance risk if there is no scenario in which the present value of cash outflows can exceed the present value of the premiums.	Same as the IASB's Exposure Draft.
5	Definition of *Acquisition Costs*	Acquisition costs are the costs incurred that vary with and are primarily related to the acquisition of new and renewal insurance contracts. However, current U.S. GAAP regarding the capitalization of acquisition costs will be amended with the proposed issuance of a final	Acquisition costs would be defined as the direct and indirect costs of selling, underwriting, and initiating an insurance contract. However, acquisition costs would be included in the cash outflows used to measure an insurance contract only if those costs are incremental (that is, those costs that would not have been incurred if	Same as the IASB's Exposure Draft.

Item		Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
		Accounting Standards Update on EITF Issue 09-G (see paragraphs 61 and 62).	the insurer had not issued that particular contract). Those costs would be identified at the level of an individual insurance contract rather than at the level of a portfolio of insurance contracts. Acquisition costs that are not identified as incremental at inception would be expensed as incurred.	
6	Definition of *Claims Liability*	The liability for unpaid claims and claim adjustment expenses is the amount needed to provide for the estimated ultimate cost required to investigate and settle claims relating to insured events that have occurred, whether or not they are reported to the insurer.	The claims liability would be the liability to pay valid claims for insured events that have already occurred, including claims incurred but not reported. Amounts would be recognized to reflect the time value of money (that is, discounted).	Same as the IASB's Exposure Draft.
7	Contract Boundaries	Contract boundaries are not explicitly defined or addressed in current U.S. GAAP.	To identify the cash flows that would be expected to arise as the insurer fulfills the obligation, it would be necessary to determine whether future premiums (and resulting benefits and claims) arise from existing contracts (included in the liability measurement) or future contracts (not included in the measurement). To make this distinction between existing and future contracts, the boundary of an insurance contract would be the point	Same as the IASB's Exposure Draft.

Item		Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
			at which an insurer either: • Is no longer required to provide coverage; or • Has the right or the practical ability to reassess the risk of the policyholder and, as a result, can set a price that fully reflects that risk.	
8	Accounting for Policyholder Behavior	Policyholder behavior, including renewal premiums and lapses, are reflected in the measurement of traditional long-duration life insurance contract liabilities. The cash flows included in the estimate of the insurance liability include the following: • Only those associated with current insurance contracts and any existing ongoing obligation to service policyholders • The value of guarantees and renewal options that provide rights under which the policyholder can obtain further contract on favorable terms. Cash flows from expected renewals that are not included within current insurance	Policyholder options, forwards, and guarantees related to existing coverage would be measured using the expected value of the net cash flows (to the extent that the cash flows are within the existing boundaries of the contract). As a result, no deposit floor would be applied. Policyholder options, forwards, and guarantees that do not relate to the existing insurance coverage would be excluded from the measurement of the contract. Rather, those instruments should be recognized and measured as either new insurance contracts or other standalone instruments according to their nature.	Same as the IASB's Exposure Draft.

	Item	Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
		contracts are excluded from the cash flows used to estimate the insurance liability. The insurance liability cannot be negative (that is, a deposit floor is applied).		
9	Unbundling	Unbundling of an insurance contract and the accounting for the components separately is required in various scenarios such as the following: • On a freestanding basis, an embedded derivative that is not clearly and closely related to the host instrument and is not already accounted for at fair value. • Annuity contracts that are considered two contracts: a deferred annuity contract in the accumulation phase and an income-pay annuity contract in the payment phase. • Partially insured or combination plans, under which the insurance policy for some of the risks related to the claims (for example, minimum premium and stop	If a component is not closely related to the insurance coverage specified in a contract, an insurer would apply other IFRSs to account for that component as if it was a separate contract (that is, it would unbundle that component). Specifically, an insurer would unbundle investment (that is, financial) and service components separately from the insurance component when there is: • A policyholder account balance that meets the following criteria: o The account balance is credited with an explicit return. o The crediting rate for the account balance is based on the investment performance of the underlying investments. • An embedded derivative that is separated from its host in accordance with existing	Same as the IASB's Exposure Draft.

Item		Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
		loss coverage), may be separately accounted for from the agreement to act as an administrator for some, or all, of the claims paid by the plan. • Certain additional liabilities for insurance-like benefits associated with variable life and annuity and universal life contracts are accounted for separately.	bifurcation guidance. • Contractual terms relating to goods and services that are not closely related to the insurance coverage but have been combined in a contract with that coverage for reasons that have no commercial substance. An insurer would not unbundle components of a contract that are closely related to the insurance coverage specified in the insurance contract. Additionally, unbundling would be prohibited except in cases in which it is required.	
10	Accounting Models/ Methods	Several methods of premium revenue and contract liability recognition for insurance contracts exist in U.S. GAAP; short-duration contract accounting and different methods of long-duration contract accounting for traditional, universal life, participating contracts, and financial guarantee contract accounting. Generally, those methods reflect the nature of the insurance entity's obligations and	The IASB's Exposure Draft proposes two approaches: one for short-duration contracts and one for long-duration contracts. A modified approach is proposed for the preclaims liabilities arising from short-duration insurance contracts (unless the contract is onerous). The measurement approach for long-duration contracts would use a building-block approach that incorporates current, discounted estimates of future cash flows remeasured at each reporting date to	The majority of the Board members support the use of a building-block approach that incorporates current, discounted estimates of net cash flows remeasured at each reporting date and a margin that is recognized over the coverage and claims handling periods (a composite margin). Several Board members expressed a preliminary view that a modified approach would be applied to some insurance

	Item	Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
		policyholder rights under the provisions of the contract. Insurance contracts are classified as short-duration or long-duration contracts depending on whether the contracts are expected to remain in force for an extended period.	reflect the effects of uncertainty about the amount and timing of future cash flows (a risk adjustment margin) and a margin that reports the profitability of the contracts over the coverage period (a residual margin). The measurement approach for claims liabilities of short-duration contracts would be measured at the present value of the fulfillment cash flows (that is, the sum of the present value of the probability-weighted net cash flows and a risk adjustment margin).	contracts (for example, certain short-duration contracts). The Board has not determined the extent to which a building-block approach or a modified approach would be applied. Additional input from stakeholders is requested in this Discussion Paper about whether different types of insurance activities warrant different accounting models. See questions 18–22.
Long-Duration Contracts				
11	Use of Model	Contracts accounted for using the long-duration model generally are not subject to unilateral changes in the contract provisions and require performance of various functions and services. Long-duration contracts typically include traditional insurance contracts (for example, whole life and term life contracts), limited-payment contracts, long-duration participating life insurance contracts, universal life-type contracts, deferred annuities, and variable and equity-based	The building-block approach described in item 10 is applicable to all contracts, except certain contracts that may use the modified approach for preclaims liabilities.	The majority of the Board members support the use of a building-block approach that incorporates current, discounted estimates of future cash flows remeasured at each reporting date and a margin that is recognized over the coverage and claims handling periods (a composite margin).

	Item	Current U.S. GAAP	IASB’s Exposure Draft	FASB’s Preliminary Views
		life and annuity products. For those contracts not explicitly referenced, if the insurance contracts have characteristics significantly similar to the previously mentioned contracts, those contracts are within the scope of the long-duration model and should be accounted for in a manner consistent with the type of contract that is the most similar. Other contracts that also should use the long-duration model are those insurance contracts that do not meet the criteria to use the short-duration model.		
12	Initial Measurement of an Insurance Contract	For traditional life and limited payment contracts, benefit liabilities are accrued on the basis of certain assumptions as premium revenue is recognized. Premium revenue generally is recognized when due except for limited-pay contracts for which gross premiums in excess of the net premium are deferred and recognized in income in a constant relationship with insurance in force.	An insurer would measure an insurance contract initially at the sum of the following: • The expected present value (unbiased and probability-weighted estimate) of the cash outflows less cash inflows that will arise as the insurer fulfills the insurance contract (discounted to adjust for the time value of money) • An adjustment for the effects of uncertainty about the amount and timing of the present value of the	An insurer would measure an insurance contract initially at the sum of the following: • The expected present value (unbiased and probability-weighted estimate) of the cash outflows less cash inflows that will arise as the insurer fulfills the insurance contract (discounted to adjust for the time value of money) • A composite margin equal to the excess of the present value of

Item	Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
	The liability for future policy benefits is measured as the present value of estimated future policy benefits to be paid to or on behalf of policyholders and related expenses less the present value of estimated future net premiums to be collected from policyholders and is accrued when premium revenue is recognized. The assumptions for measuring traditional life insurance benefit liabilities (such as investment return, mortality, termination, and expense assumptions) are locked in at inception and unlocked or reset only if a premium deficiency emerges. The discount rate is based on the estimated pre-tax investment yields (net of related invested expenses) expected at the contract issue date, adjusted for adverse deviation. For long-duration participating contracts, policyholder benefits are measured as the excess of the present value of future guaranteed death and endowment benefits over the	fulfillment cash flows (risk adjustment margin) • A residual margin that eliminates any gain at initial recognition of the contract. A residual margin arises when the sum of the expected present value and the risk adjustment is less than zero (that is, when the expected present value of the cash outflows plus the risk adjustment margin is less than the expected present value of the cash inflows).	cash inflows over the present value of cash outflows (unless the contract is onerous).

Item		Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
		present value of future net premiums. Additionally, a liability is accrued for terminal dividends when the payment of the dividend is probable and the amount can be reasonably estimated. For universal life-type contracts, deferred annuities and variable and equity-based life and annuity products, the liability is equal to the account balance if one exists or an implicit account balance or the cash value available for the policyholder, plus other adjustments.		
13	Initial Measurement of a Risk Adjustment	For traditional and long-duration participating life insurance contracts, a provision for the risk of adverse deviation is included in the measurement of the liability for future claims and policy benefits. The provision for the risk of adverse deviation allows for possible unfavorable deviations from assumptions (which are not revised unless there is a premium deficiency), such as estimates of expected investment yields, mortality, morbidity, terminations, and	The risk adjustment margin would represent the maximum amount that the insurer would rationally pay to be relieved of the risk that the ultimate fulfillment cash flows exceed those expected. An insurer would estimate the risk adjustment margin at the level of a portfolio of insurance contracts. Therefore, the risk adjustment margin would reflect the effects of diversification that arise within a portfolio of insurance contracts, but it would not reflect the effects of diversification between that portfolio and other portfolios of insurance	The measurement of an insurance contract would not include a separate risk adjustment margin and residual margin but, instead, combine them in a single composite margin. See item 14, Initial Measurement of a Residual Margin (IASB) and a Composite Margin (FASB).

Item		Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
		expenses. The liabilities related to universal life-type contracts, deferred annuities, and variable and equity-based life and annuity products do not contain a provision for adverse deviation.	contracts. The risk adjustment margin would provide a means for depicting the uncertainty in possible outcomes and insight into management's perception of the uncertainty. It would measure explicitly how much risk is present in the liability. The risk adjustment margin would be remeasured each period (using one of the techniques in paragraph 75) and would reflect changes in the maximum amount the insurer would rationally pay to be relieved of the risk that the ultimate fulfillment cash flows exceed those expected.	
14	Initial Measurement of a Residual Margin (IASB) and a Composite Margin (FASB)	For traditional and long-duration participating insurance contracts, the profit on the contract is embedded in the policyholder liability and the unamortized acquisition costs. For universal life-type contracts, deferred annuities, and variable and equity-based life and annuity products, the profit on the contract is embedded in the account value and the unearned revenue liability. A gain is not recognized upon	The residual margin would be calibrated at initial recognition in such a way that an insurer would not recognize a gain upon entering into an insurance contract. The residual margin would be recognized in earnings over the coverage period in a systematic manner on the basis of the passage of time, unless the pattern of claims and benefits makes another pattern more appropriate.	Risk associated with the uncertainty in cash flows of an insurance contract would be considered in that contract's pricing and, therefore, would be implicit in the composite margin. The composite margin would represent the amount necessary to eliminate any gain at initial contract recognition. That amount would be measured as the difference between the present value of the expected premiums and the present value of the expected claims, benefits, and

Item		Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
		inception of a contract.		expenses. The composite margin would be recognized in earnings over both the coverage and claims-handling periods to reflect the insurer's exposure to uncertainties related to the amount and timing of future cash flows.
15	Initial Measurement of Cash Flows	Cash flows are included only for current insurance contracts and any existing ongoing obligation to service policyholders. For traditional life insurance contracts, the present value of estimated future policy benefits and related expenses and the present value of estimated future net premiums consider all cash flows related to the contract. For long-duration participating contracts, the present value of future guaranteed death and endowment benefits, the present value of future net premiums, and the terminal dividend liability consider all cash flows related to the contract. In addition, the estimated gross margin calculation used for the subsequent measurement of	At initial recognition, an insurer would include in the measurement of the insurance contract an estimate of all cash flows that arise as the insurer fulfills the insurance contract over the life of that contract. An insurer would adjust the future cash flows for the time value of money using the current discount rate. Some of those cash flows would be received or paid on the day that the insurance contract is initially recognized, for example, initial premiums and some incremental acquisition costs. Those cash flows would result in a change in the carrying amount of the insurance liability immediately after that initial recognition and not on the day that the insurance contract is initially recognized.	Same as the IASB's Exposure Draft.

Item		Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
		deferred acquisition costs considers all cash flows related to the contract. For universal life-type contracts, deferred annuities and variable and equity based life and annuity products, the estimated gross profit calculation used for the subsequent measurement of deferred acquisition costs, considers all cash flows related to the contract.		
16	Initial Measurement of Acquisition Costs	Acquisition costs are capitalized as an asset. Acquisition costs are those costs that vary with and are primarily related to the acquisition of new and renewal insurance contracts. Acquisition costs generally include commissions, premium taxes, salaries of certain employees involved in the underwriting and policy issue functions, and medical and inspection fees. Other costs incurred during the period, such as those relating to investments, general administration, policy maintenance, product	Incremental acquisition costs would be included in the measurement of the present value of the fulfillment cash flows (at the individual contract level). As a result, those costs would affect earnings over the coverage period, rather than at initial recognition. Acquisition costs that are not identified as incremental at initial recognition of the contract would be expensed as incurred.	Same as the IASB's Exposure Draft, except references to the present value of the fulfillment cash flows would be replace with the present value of the probability-weighted estimate of net cash flows.

Item		Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
		development expenses, market research expenses, and general overhead, that do not vary with and are not primarily related to the acquisition of new and renewal insurance contracts are charged to expense as incurred. However, current U.S. GAAP regarding the capitalization of acquisition costs will be amended with the issuance of a final Accounting Standards Update on EITF Issue 09-G (see paragraphs 61 and 62).		
17	Subsequent Measurement of an Insurance Contract	For traditional life insurance contracts, at each reporting period, the liability for future policy benefits is measured as the present value of estimated future policy benefits to be paid to or on behalf of policyholders and related expenses less the present value of estimated future net premiums to be collected from policyholders. The liability for future policy benefits is accrued when premium revenue is recognized. For long-duration participating contracts, at each reporting	The carrying amount of the insurance contract would be remeasured at the end of each reporting period as the sum of the present value of the net fulfillment cash flows at that date (including the risk adjustment margin) and the remaining amount of the residual margin. The present value of the fulfillment cash flows would reflect all available information as of the end of the reporting period. Estimates of cash flows in a scenario would include all cash flows within the boundary of an existing contract that are incremental at the level of a portfolio of insurance	Similar to the IASB, except for the following: • The carrying amount of the insurance contract would be measured at the end of each reporting period as the sum of the present value of the net cash flows at that date • The remaining amount of the composite margin and references to the present value of the fulfillment cash flows would be replaced with the present value of the probability-weighted estimate of net cash flows.

Item	Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
	period, the liability for policyholder benefits is measured as the excess of the present value of future guaranteed death and endowment benefits over the present value of future net premiums. The original assumptions used when the contracts are issued are locked in and, thus, used in all future liability calculations as long as the resulting liabilities are adequate to provide for the future benefits and expenses under the related contracts. Changes in the liability for future policy benefits are recognized in income of the period in which changes occur. Terminal dividends related to long-duration participating contracts are recognized as an expense over the life of a book of participating life insurance contracts, at a constant rate based on the present value of the estimated gross margin amounts expected to be realized over the life of the book of	contracts, and no others. Cash outflows that are incremental to a portfolio of insurance contracts would include direct costs and systematic allocations of costs that relate directly to the insurance contracts or contract activities.	.

Item	Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
	contracts. For universal life-type contracts and deferred annuities, the unearned revenue liability (amounts assessed that represent compensation to the insurance enterprise for services to be provided in future periods) are recognized in income over the period benefited using the same assumptions and factors used to amortize capitalized acquisition costs. The additional liability recorded for insurance contracts in which an insurance benefit feature results in an expectation of profits in the early years followed by losses in the later years is recognized in earnings similar to the amortization of capitalized acquisition costs. The benefit ratio is readjusted at each reporting period for actual and current future projections. For all long-duration insurance contracts, liabilities for unpaid claims and claims adjustment expenses are accrued when insured events occur.		

	Item	Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
18	Subsequent Measurement of a Risk Adjustment Margin	For traditional and long-duration participating life insurance contracts, the provision for the risk of adverse deviation included in the measurement of the liability for future claims and policy benefits is recognized as a result of experience under the contract.	The risk adjustment margin would be explicitly remeasured at the end of each reporting period over the coverage and claims handling periods using either the confidence level, conditional tail expectation, or cost of capital technique. The risk adjustment margin would decline over time as the insurer is released from risk but, in principle, could increase or decrease at the end of each reporting period.	The measurement of an insurance contract would not include a separate risk adjustment margin and residual margin, but would instead combine them in a single composite margin. See item 14, Initial Measurement of a Residual Margin (IASB) and a Composite Margin (FASB).
19	Subsequent Measurement of a Residual Margin (IASB) and a Composite Margin (FASB)	A similar concept does not exist in current U.S. GAAP.	An insurer would recognize the residual margin determined at initial recognition as income in earnings over the coverage period in a systematic way that best reflects the exposure from providing insurance coverage. An insurer would accrete interest on the carrying amount of the residual margin using the current discount rate at initial recognition. The residual margin would not be remeasured in subsequent periods as a result of changes in cash flow estimates.	The composite margin would be recognized in earnings considering the insurer's exposure relating to the provision for insurance coverage and to the uncertainties in the cash flows. Therefore, the composite margin would be recognized in earnings over the coverage and claims handling periods. The ratio applied to the composite margin would be as follows: (Premiums allocated to date + Claims and benefits paid to date) ÷ (Total expected premiums + Total expected claims and benefits) The composite margin would not be remeasured in subsequent

Item		Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
				reporting periods for changes in cash flow estimates. However, the portion of the composite margin recognized in earnings would vary over the coverage and claims handling periods because the ratio would be updated each period for actual claims and benefits paid during the period and changes in expected cash flows. Interest would not be accreted on the composite margin.
20	Subsequent Measurement of Acquisition Costs	For traditional long-duration contracts, capitalized acquisition costs are amortized according to a percentage of premiums. For universal life-type contracts, deferred annuities, and variable and equity-based life and annuity products, capitalized acquisition costs are amortized according to a percentage of estimated gross profits. Estimated gross profits used to amortize acquisition costs are updated for actual experience and current future projections each reporting period. For certain investment contracts, capitalized acquisition costs are	Because incremental acquisition costs would be included in the measurement of the present value of the fulfillment cash flows, the amount of residual margin would be correspondingly lower and, therefore, those costs would affect earnings over the coverage period but would not be explicitly amortized.	Same as the IASB's Exposure Draft, except for the following: • References to the present value of the fulfillment cash flows would be replaced with the present value of the probability-weighted estimate of net cash flows • The IASB would recognize the residual margin over the coverage period and the Board would recognize the composite margin over the coverage and claims handling periods.

Item		Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
		amortized using the interest method. That method recognizes acquisition and interest costs as expenses at a constant rate to net policy liabilities. For long-duration participating life insurance contracts, capitalized acquisition costs are amortized over a percentage of estimated gross margins. Estimated gross margins used to amortize acquisition costs are updated for actual experience and current future projections each reporting period.		
21	Subsequent Measurement Using an Onerous Test	A premium deficiency exists if the liability for future policy benefits at the valuation date (reduced by unamortized acquisition costs) is less than the liability for future policy benefits using revised assumptions (on the basis of actual and anticipated experience). The premium deficiency test is performed on a group of insurance contracts consistent with the entity's manner of acquiring, servicing, and measuring the profitability of its	The carrying amount of the insurance contract would be remeasured at the end of each reporting period, and changes would be recognized in earnings. Therefore, a separate onerous test would not be necessary.	Same as the IASB's Exposure Draft.

Item		Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
		insurance contracts. A premium deficiency is recognized by either a reduction in unamortized acquisition costs or an increase in the policyholder benefits.		
Short-Duration Contracts				
22	Use of Model	Short-duration contracts are those that provide insurance protection for a fixed period of short duration and that enable the insurer to cancel the contract or to adjust the provisions of the contract at the end of the contract period. The period of short duration is not explicitly defined in U.S. GAAP, but in practice is generally one year or less. Two main aspects of the short-duration insurance contract model are that (1) the premium is recognized as revenue over the period of the contract in proportion to the amount of insurance protection provided and (2) a claims liability is measured as claims are incurred, whether or not those claims have	Short-duration contracts would be those that meet the following conditions: • The coverage period of the insurance contract is approximately one year or less. • The contract does not contain embedded options or other derivatives that significantly affect the variability of cash flows, after unbundling any embedded derivatives.	Several Board members expressed a preliminary view that a modified approach would be applied to some insurance activities (for example, certain short-duration contracts). The Board has not determined the extent to which a building-block approach or a modified approach would be applied. Additional input from stakeholders is requested in this Discussion Paper about whether different types of insurance activities warrant different accounting models. See questions 18–22.

	Item	Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
		been reported. Short-duration contracts give rise to two distinct liabilities: the unearned premiums (preclaims liability) and the claims liability. The unearned premiums represent the insurance entity's obligation during the coverage period to stand ready to perform in accordance with the insurance contract. The claims liability represents the unconditional requirement to perform in accordance with to the insurance contract after an insured event has occurred.		
23	Initial Measurement of a Preclaims Liability	The unearned premiums provide for future events and expenses arising under existing contracts, that is, a preclaims liability for unexpired contract terms.	The preclaims obligation would equal the premium received at initial recognition plus the expected present value of future premiums within the boundary of the existing contract less incremental acquisition costs.	Similar to the IASB's Exposure Draft, except the Board has not decided whether incremental acquisition costs would reduce the preclaims liability.
24	Initial Measurement of Acquisition Costs	Acquisition costs are capitalized as an asset and amortized over the life of the contract. Acquisition costs are those costs that vary with and are primarily related to the acquisition of new and renewal insurance contracts.	Incremental acquisition costs would reduce the measurement of the preclaims obligation, which would subsequently be recognized in earnings over the coverage period in a systematic way. Thus, deferred acquisition costs would be presented as a reduction of the preclaims	The Board has not decided whether incremental acquisition costs would reduce the preclaims liability.

	Item	Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
		Acquisition costs generally include commissions, premium taxes, salaries of certain employees involved in the underwriting and policy issue functions, and medical and inspection fees. Other costs incurred during the period, such as those relating to investments, general administration, policy maintenance, product development expenses, market research expenses, and general overhead, that do not vary with and are not primarily related to the acquisition of new and renewal insurance contracts are charged to expense as incurred. However, current U.S. GAAP regarding the capitalization of acquisition costs will be amended with the issuance of a final Accounting Standards Update on EITF Issue 09-G (see paragraphs 61 and 62).	liability. Acquisition costs that are not incremental at initial recognition would be expensed as incurred.	
25	Subsequent Measurement of the Allocation of Premiums	Premiums are recognized as revenue over the period of the contract in proportion to the amount of insurance protection	Premiums would be recognized over the coverage period in a systematic way that best reflects the insurer's exposure to risk from providing	Same as the IASB's Exposure Draft.

Item		Current U.S. GAAP	IASB's Exposure Draft	FASB's Preliminary Views
		provided.	insurance coverage, as follows: • On the basis of the passage of time, but • On the basis of the expected timing of incurred claims and benefits if that pattern differs significantly from the passage of time.	
26	Subsequent Measurement of a Preclaims Liability	The remaining unearned premiums represent the preclaims liability for unexpired contract terms. Discounting is not addressed in Topic 944, but current practice is not to discount short-duration preclaims liabilities.	The remaining unearned premiums (less unamortized incremental acquisition costs) would be the preclaims liability for unexpired contract terms. Interest would be accreted on the carrying amount of the preclaims liability using the current discount rate.	Similar to the IASB's Exposure Draft, except the Board has not decided whether incremental acquisition costs would reduce the preclaims liability or whether interest would be accreted on the carrying amount of the preclaims liability.
27	Subsequent Measurement of Acquisition Costs	Acquisition costs are charged to expense in proportion to premium revenue recognized.	Because incremental acquisition costs would reduce the preclaims obligation, those costs would affect earnings in a systematic manner that best reflects the insurer's exposure to risk from providing insurance coverage. The amortization of incremental acquisition costs would be presented or disclosed separately each reporting period.	The Board has not decided whether incremental acquisition costs would reduce the preclaims liability.

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28	Subsequent Measurement of a Claims Liability	The liability for unpaid claims is based on the undiscounted best estimates, using past experience adjusted for current trends, of the ultimate expected claims payments for incurred losses including claims that have been reported to the insurer and claims relating to insured events that have occurred but have not been reported to the insurer as of the date the liability is estimated. Following an insured event, the insurance entity accrues a liability for unpaid claims and a liability for claims adjustment expenses. Current practice is generally not to discount short-term liabilities.[17]	As insured events occur, the claims liability would be measured at the present value of the fulfillment cash flows.	Similar to the IASB's Exposure Draft, except references to the present value of the fulfillment cash flows would be replaced with the present value of the probability-weighted estimate of net cash flows (that is, an explicit risk adjustment margin would not be included).
29	Subsequent Measurement Using an	Contracts are tested each period for premium deficiency by comparing the sum of expected	A contract would be onerous if the present value of the fulfillment cash flows relating to future insured claims	Similar to the IASB's Exposure Draft, except references to the present value of the fulfillment

[17] As explained in the U.S. Securities and Exchange Commission's (SEC) Staff Accounting Bulletin Topic 5N, *Discounting By Property-Casualty Insurance Companies*, the SEC staff does not object to discounting liabilities for unpaid claims and claims adjustment expenses at the same rates that an entity uses for reporting to state regulatory authorities with respect to the same claims liabilities. The SEC staff also does not object to discounting liabilities with respect to settled claims as long as the payment pattern and ultimate cost are fixed and determinable on an individual claim basis and the discount rate used is reasonable based on the facts and circumstances applicable to the entity at the time the claims are settled.

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	Onerous Test	loss, loss expenses, and acquisition costs to the remaining unearned premiums. A premium deficiency is recognized by expensing any unamortized acquisition costs to the extent required to eliminate the deficiency. If the premium deficiency is greater than unamortized acquisitions costs, a liability is accrued for the excess deficiency.	exceeds the carrying amount of the preclaims obligation. If the contract is determined to be onerous, the insurer would recognize an additional liability and the loss in earnings. The additional liability would be remeasured each reporting period and reversed when the preclaims obligation exceeds the present value of the fulfillment cash flows.	cash flows would be replaced with the present value of the probability-weighted estimate of net cash flows (that is, an explicit risk adjustment margin would not be included).
Reinsurance				
30	Reinsurance	The accounting provisions for reinsurance contracts depend on whether the contracts are long or short duration and, if short duration, on whether the contracts are considered prospective or retroactive reinsurance contracts. Regardless of its form, any transaction that indemnifies an insurer against loss or liability relating to insurance risk is accounted for in Topic 944. Reinsurance contracts that are legal replacements of one insurer by another (often referred to as	A reinsurance contract is an insurance contract issued by one insurer (the reinsurer) to compensate another insurer (the cedant) for losses on one or more contracts issued by the cedant. A reinsurer would use the same recognition and measurement approach for reinsurance contracts that is used for direct insurance contracts. A cedant would measure a reinsurance contract at initial recognition as the sum of: • The present value of the fulfillment	References to *residual margin* would be replaced with *composite margin*. Additionally, references to the present value of the fulfillment cash flows would be replaced with the present value of the probability-weighted estimate of net cash flows (that is, an explicit risk adjustment margin would not be included).

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	assumption and novation) extinguish the ceding enterprise's liability to the policyholder and result in removal of related assets and liabilities from the financial statements of the ceding enterprise. Reinsurance contracts in which a ceding enterprise is not relieved of the legal liability to its policyholder do not result in removal of the related assets and liabilities from the ceding enterprise's financial statements. Ceding enterprises report estimated reinsurance receivables arising from those contracts separately as assets. Amounts paid to the reinsurer relating to the unexpired portion of reinsured contracts (prepaid reinsurance premiums) also are reported separately as assets. Reinsurance receivables and prepaid reinsurance premiums are recognized in a manner consistent with the related liabilities (estimates for claims incurred but not reported and future contract/policy benefits) relating to the underlying insurance contracts.	cash flows (the expected present value of the cedant's future cash inflows plus the risk adjustment margin less the expected present value of the cedant's future cash outflows) • A residual margin. The cedant would estimate the present value of the fulfillment cash flows in the same manner as the corresponding part for the present value of the fulfillment cash flows for the underlying insurance contract. Additionally, the cedant would consider the risk of nonperformance by the reinsurer on an expected value basis when estimating the present value of the fulfillment cash flows. The cedant would treat ceding commissions it receives as a reduction of the premium ceded to the reinsurer. If the future cash inflows plus the risk adjustment margin exceed the future cash outflows, a gain would be recognized in earnings. However, if the future cash inflows plus the risk adjustment margin are less than the future cash outflows, the cedant would recognize the difference in the residual margin.	

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		Assumptions used in estimating reinsurance receivables must be consistent with those assumptions used in estimating the related liabilities. Under certain kinds of reinsurance agreements, the acquisition expenses that are reimbursed by the assuming entity are offset against the ceding entity's deferred acquisition costs. Amounts receivable and payable between the ceding enterprise and an individual reinsurer are offset only when a right of setoff exists, as defined in Subtopic 210-20, Balance Sheet—Offsetting. The amounts of earned premiums ceded and recoveries recognized under reinsurance contracts either are reported in the statement of earnings, as separate line items or parenthetically, or those amounts are disclosed in the footnotes to the financial statements. Reinsurance contracts do not result in immediate recognition of gains unless the reinsurance contract is a legal replacement of		

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		one insurer by another and thereby extinguishes the ceding enterprise's liability to the policyholder. More extensive guidance for reinsurance contracts is in Topic 944.		
Presentation				
31	Statement of Comprehensive Income for Long-Duration Contracts	U.S. GAAP contains limited explicit guidance on presentation but does include extensive examples and illustrations. The presentation requirements are driven primarily by SEC Regulations. For traditional life, any gross premiums received in excess of the net premiums are deferred and recognized in earnings in a constant relationship with insurance in force (for life insurance contracts) or with the amount of expected future benefit payments (for annuity contracts). For universal life-type contracts, deferred annuities, and variable and equity-based life and annuity products, premiums are not presented as revenue and	An insurer would present income and expense using a margin presentation approach in a manner that highlights the following: • The underwriting margins (that is, changes in the risk adjustment margin and recognition of the residual margin in earnings) • Changes in estimates (that is, differences between actual cash flows and previous estimates, and changes in current estimates of cash flows and discount rates) • Interest related to insurance liabilities (presented or disclosed in a way that highlights its relationship with the investment return on assets backing those liabilities). An insurer would be required to present all income and expense arising from insurance contracts in earnings. However, an insurer would	In the Board's view, the measurement approach should drive the presentation approach for the statement of comprehensive income and tentatively agrees with the margin presentation approach proposed by the IASB. An insurer would present income and expense for insurance contracts using a margin presentation showing the recognition in earnings of the composite margin, differences between the expected and the actual cash flows, changes in estimates, and interest on the carrying amount of insurance contracts. An insurer would treat premiums as deposits and claims expenses, claims handling expenses, and

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		payments to policyholders are not presented as expenses. Instead, amounts assessed against policyholders (for example, cost of insurance, surrender charges, policy fees, and other charges) are presented as revenues and are recognized in the period received or over the period benefited. Items presented as expenses include benefit claims in excess of account balances, costs of contract administration, interest credited to policyholder balances, and amortization of deferred acquisition costs.	not present premiums, which instead would be treated in the same way as deposit receipts, claims expenses, claims handling expenses, incremental acquisition costs, and other expenses included in the measurement of the insurance contract, which instead would be treated in the same way as repayments of deposits.	other contract-related expenses as repayments of deposits.
32	Statement of Comprehensive Income for Short-Duration Contracts	U.S. GAAP contains limited explicit guidance on presentation but does include extensive examples and illustrations. The presentation requirements are driven primarily by SEC Regulations.	An insurer using a modified approach for measurement would use the premium allocation presentation approach and would present the following amounts each period: • The underwriting margin, disaggregated either in the statement of comprehensive income or in the notes as follows: o Premium revenue, determined as the allocation of the preclaims obligation to the reporting period (less incremental	Similar to the IASB's Exposure Draft, except the Board has not decided whether incremental acquisition costs would reduce the preclaims liability. As a result, the Board has not decided the manner in which incremental acquisition costs would be presented in the statement of comprehensive income for short-duration contracts.

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			acquisition costs) o Claims incurred o Expenses incurred o Amortization of incremental acquisition costs included in the preclaims obligation. • Changes in additional liabilities for onerous contracts.	
33	Statement of Financial Position for Both Long- and Short-Duration Contracts	U.S. GAAP contains limited explicit guidance on presentation but does include extensive examples and illustrations. The presentation requirements are driven primarily by SEC Regulations.	The IASB proposes a margin presentation approach in which the combination of rights and obligations arising from an insurance contract would be presented net as a single insurance contract asset or liability in the statement of financial position, consistent with the measurement of an insurance contract asset or liability on the basis of a package of cash inflows and outflows. As such, an insurer would present each portfolio of insurance contracts as a single item within insurance contract assets or insurance contract liabilities.	Same as the IASB's Exposure Draft.
Disclosure				
34	General	U.S. GAAP contains explicit disclosure guidance depending on the type of insurance contract. Additionally, it includes extensive examples and illustrations.	The objective of the proposed disclosure requirements is to help users of financial statements understand the amount, timing, and uncertainty of cash flows arising from insurance contracts. An insurer would	Same as the IASB's Exposure Draft.

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	General disclosures required for insurance contracts include the following: • The basis for estimating the liabilities for unpaid claims and claims adjustment expenses • The nature of acquisition costs capitalized, the method of amortizing capitalized acquisition costs, and the amount of acquisition costs amortized for the period • A reconciliation of the beginning and ending balances for the liability for unpaid claims and claims adjustment expenses • Payments of claims and claims adjustment expenses.	disclose qualitative and quantitative information about amounts recognized in its financial statements arising from insurance contracts and the nature and extent of risks arising from insurance contracts. An insurer would disclose information in sufficient detail to help users of its financial statements evaluate the timing, amount, and uncertainty of future cash flows arising from insurance contracts, including a reconciliation of the opening and closing aggregate contract balances as well as the methods and inputs used to develop the measurements.	