



Letter of Comment No: 7
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AMERICAN ACADEMY of ACTUARIES

March 22, 2004

Robert H. Herz, Chairman
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, Connecticut 06856-5116

***Re: EIL 04-08, Accounting for Unearned Revenue Liabilities related to a
FASB Statement No. 97 Universal Life-Type Contract with Death or
Other Insurance Benefit Features***

Dear Mr. Herz,

The American Academy of Actuaries' (Academy) Life Financial Reporting Committee (LFRC) is pleased to have this opportunity to comment on EIL 04-08, *Accounting for Unearned Revenue Liabilities related to a FASB Statement No. 97 Universal Life-Type Contract with Death or Other Insurance Benefit Features*. The LFRC appreciates the effort you are making to clarify how paragraph 26 of SOP 03-1, *Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts*, should be applied to universal life and variable universal life insurance contracts.

EIL 04-08 addresses a very specific issue. Consider a universal life-type insurance contract with cost of insurance ("COI") charges assessed in a manner that is expected to result in profits in earlier years followed by smaller amounts of profits in subsequent years. In this context, 'profits' is understood to be the excess of COI charges over expected insurance benefit payments and related claim adjustment expenses, without considering other sources of margin. The question asked in EIL 04-08 is whether or not a company may determine it appropriate to defer a portion of COI charges in early years as unearned revenue. One view (View A) is that such deferral is prohibited. The other view (View B) is that deferral is not prohibited; deferral is appropriate in situations where evidence exists that COI charges in early years include amounts for benefits to be paid or services to be provided in future periods. Proponents of both views point to the discussion in paragraphs 60 & 61 of FASB Statement No. 97 (FAS 97) for support.

From an actuarial perspective, we would like to indicate our support for View B. We feel View B well articulates the appropriateness of holding an unearned revenue liability for certain COI charges where warranted by the facts and circumstances. We feel current practice appropriately addresses the issue in View B of deferring only those portions of COI charges which provide for future benefits or services, and of not deferring other portions of COI charges simply to 'smooth' out margins. As a corollary, we feel View A could lead to unintended inconsistencies or manipulation, for example, based on whether an expense load is explicitly applied or implicitly included in identical amount within the COI scale. Specifically, we feel it may be inappropriate to base a decision on deferability of an item solely on its categorization rather than on a consideration of the economic facts.

In closing, we again want to thank you for giving us the opportunity to share our views. Please note that our response is in regard to the very narrow issue raised by EIL 04-08 and we would be happy to assist in any further developments in interpretation of other issues raised in regard to SOP 03-1 and FAS 97. If you have any questions, or need additional clarification, please contact Steve English, the Academy's senior life policy analyst (telephone 202-785-7880, english@actuary.org) or me (telephone 847-402-7651, ecramer@allstate.com).

Sincerely,

A handwritten signature in black ink, appearing to read "Errol Cramer". The signature is fluid and cursive, with a large initial "E" and "C".

Errol Cramer, Chairperson – Life Financial Reporting Committee
American Academy of Actuaries

Cc: Mark Beilstein, Chairman
Accounting Standards Executive Committee
Gary S. Schieneman, Board Member
Financial Accounting Standards Board

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