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International Accounting Standards Board 30 Cannon Street London, EC4M 6XH United Kingdom Financial Accounting Standards Board 401 Merritt 7 P.O. Box 5116 Norwalk, Connecticut 06856-5116

## **Re: Exposure Draft on Insurance Contracts**

The American Insurance Association (AIA) is the leading property-casualty insurance trade organization, representing approximately 300 insurers that write more than \$117 billion in premiums each year. AIA member companies offer all types of property - casualty insurance, including personal and commercial auto insurance, commercial property and liability coverage for small businesses, workers' compensation, homeowners' insurance, medical malpractice coverage, and product liability insurance. We have been closely following the Insurance Contracts activity of the International Accounting Standards Board ("IASB") and the Financial Accounting Standards Board ("FASB") (collectively, the "Boards") for some time and we provided comments on the IASB's 2007 discussion paper, *Preliminary Views on Insurance Contracts*. When the Boards issue an Exposure Draft or a Discussion Paper ("ED") on Insurance Contracts, we will again provide comments because we believe it is imperative that the Boards understand the implications of an ED from the perspective of property and casualty insurers.

We are pleased the FASB joined the IASB's Insurance Contracts project in 2008 and believe the joint discussions have added valuable insight and viewpoints to the debate. However, we are deeply concerned that the IASB plans to release the Insurance Contracts ED at a time when the respective Boards hold different views on a number of important technical issues. It is our understanding that the IASB's insurance contracts ED may present alternative views on issues where the Boards have reached divergent conclusions. If this is the case, it will be difficult for stakeholders to adequately respond to the insurance ED and, likewise, for the Boards to evaluate and interpret the comments received. The inclusion of alternative views increases the complexity of assessing the various alternatives.

The various technical issues being considered are inter-connected and therefore cannot really be effectively evaluated separately. One would need to imagine the potential combinations of components that might be used (and there would be many) in order to identify the meaningful issues associated with any one overall approach. If the IASB proceeds with issuing an ED with

alternative views, respondents would need to evaluate each component independently of knowledge about the overarching framework and/or principles of a full standard, including how the information would be presented in financial statements. Without an overall context of how interrelated parts would fit together, comments will not be made in the context of a single comprehensive standard and there is a significant risk that the Boards will reach inappropriate and erroneous conclusions based on the respondents' comments.

An ED is usually presented in the form of a proposed standard that, if no changes are deemed necessary, could be adopted as drafted. Issuing an ED with various alternatives for measurement and presentation, however, is an unprecedented approach in releasing an ED and, depending on the IASB's decision to make changes and re-expose for comment, could raise process and transparency issues. At a minimum, we believe the IASB would need to publish a revised exposure draft so that stakeholders would have an opportunity to review and comment on the actual standard that is being considered for adoption.

Further, a high quality accounting standard for insurance contracts must reflect the characteristics of insurance contracts and the nature of the insurance business. However, we believe that the building blocks approach, in particular the application of probability-weighted cash flows, cannot be applied in the context of measuring property and casualty claims liabilities. For example, the inherently uncertain aspects of the liability products of property and casualty insurers – such as the uncertainty of a claim-generating occurrence, the timing of claim presentation, the cost of defending the insured, the amount to satisfy the claim, and the timing of the claim payment – cannot and will not become more certain by creating a subjective array of probability—weighted cash flows. In effect, the proposed approach would require omniscience with regard to the possible outcome of uncertain events, including unpredictable human behavior that leads to unusual jury awards and new judicial interpretations of insurance policy language.

For property and casualty insurers, a variety of well-accepted actuarial methods are currently used to establish a mean estimate of claims liabilities, rather than attempting to estimate all possible scenarios and assigning probability-weights to each scenario. The subjectivity and uncertainty associated with assigning the appropriate probability-weights to all possible scenarios would far exceed the subjectivity and uncertainty associated with utilizing a mean estimate. As such, the proposed methodology is not practical to implement.

We are concerned that the characteristics that are unique to the property and casualty insurance business model have not been adequately considered and addressed in the Boards' deliberations; a fuller understanding of property and casualty insurance issues could help resolve some of the outstanding issues that have resulted in the alternative views. Accordingly, we encourage the Boards to seek further dialogue with the insurance industry to assist in resolution of some of the most critical differences before issuing the Insurance Contracts ED. After an insurance contracts ED is issued, we encourage the Boards to work together to develop a process for evaluating the feedback received, which should include conducting public roundtables.

We support the issuance of a high quality standard based on a proposal that is completed with sufficient consideration of insurance industry comments and the benefit of field testing. It is important to conduct field testing and modeling of results under the final proposal. Failure to field test and model the results creates the risk of issuing a final standard that, in our view, may not reflect the property and casualty insurance business model and could materially mislead users of insurance company financial statements.

Finally, both Boards should consider the need to synchronize their decisions on the financial instruments project with the decisions of the insurance contracts project. As major investors in financial instruments, insurers must understand the impact on the asset side of their balance sheets, as well as the impact the insurance contract ED will have on the liabilities side. In order to provide the most useful feedback to both Boards, insurers must be able to concurrently field test both the ED for insurance contracts and the ED for financial instruments.

In summary, we believe the alternative views approach of issuing an ED will not be helpful and will create further delays. If a comprehensive proposal is not presented in the ED, it will be necessary to issue a second exposure draft, followed by the same public due process period, thus resulting in significant delay in the timeline for issuing a final standard. We also recommend that the Boards seek insurance industry assistance to resolve the outstanding issues between the Boards, with particular consideration on the relevance of those issues to the property and casualty insurance industry. Finally, we cannot over-emphasize the importance of allowing time for field testing and modeling of both the financial instruments ED and the insurance contracts ED, in order to provide assurance that the proposed standards are workable and adequately reflect the business models of the P&C insurance industry.

AIA member companies are interested in having a dialogue on how to best achieve the Boards' critical objectives within the timeframes available to them for finalizing the insurance contracts and financial instruments standards. We offer our assistance and look forward to working with the Boards. We hope you find our comments to be helpful and we would be pleased to further discuss our concerns. Please feel free to contact us with any questions.

Sincerely,

Phillip L. Carson

**Assistant General Counsel** 

Thillip S. Carsoz