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1325-100

LETTER OF COMMENT NO. 38

Microsoft

August 24, 2006

Ms. Suzanne Bielstein
Director of Major Projects and Technical Activities
Financial Accounting Standards Board
401 Merritt 7
Norwalk, CT 06856-5116

Re: File Reference No. 1325-100

Dear Sue:

Microsoft appreciates the opportunity to respond to the Invitation to Comment (IC), "Bifurcation of Insurance and Reinsurance Contracts for Financial Reporting". As a corporate entity that purchases commercial insurance, our comments are framed from the perspective of a buyer of insurance, and we have tried to avoid commenting on insurer or reinsurer accounting. We do not believe a requirement to bifurcate insurance contracts will improve financial reporting. Rather, we believe a bifurcation requirement is likely to result in arbitrary allocations and would not result in more representationally faithful financial statements. Furthermore, a requirement to bifurcate would require significant and costly systems changes. Given the IASB's ongoing Insurance Contracts project, Microsoft recommends that the FASB converge with the guidance in IFRS 4, *Insurance Contracts.*

IFRS 4 requires that a contract be accounted for as insurance if it transfers significant insurance risk. 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. IFRS 4 provides examples of insurance contracts as well as examples of the application of the definition of an insurance contract. Unlike U.S. GAAP, this guidance more appropriately defines insurance risk by the nature of the events or occurrences that can trigger a claim and the obligation to compensate for the loss.

Microsoft believes this approach is superior to a mathematical approach based on estimates of future outcomes. We also believe it will obviate the current concern that contracts that transfer only limited insurance risk are being accounted for as insurance contracts. However, similar to IFRS 4, we believe that bifurcation is appropriate for insurance contracts containing both an insurance component and a deposit component, provided the deposit component is unambiguously separable as defined by the contract terms.

While it is currently being applied by corporate policyholders due to the lack of other guidance, we do not believe it is reasonable to expect the guidance in FASB Statement 113, *Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts,* to produce sufficiently credible and accurate risk estimates for a corporate policyholder. The situation of a corporate policyholder is not comparable to that of an insurer, where the insurer may be reinsuring a book of thousands of homogeneous insurance policies and the law of large numbers therefore allows a far more accurate risk estimate.

Microsoft also disagrees with the concept that any loss below the level of expected loss is not real risk transfer, but only "dollar trading", and therefore should be treated as a deposit. As previously indicated, we believe the guidance in IFRS 4 more appropriately defines insurance risk by the nature of the events or occurrences that can trigger a claim and the obligation to compensate for the loss. For instance, paragraph B18 of IFRS 4 specifically classifies disability and medical coverage as insurance, without regard to whether they are group or individual policies.

Our responses to the individual issues raised in the IC are attached. If you have any questions, please contact me at (425) 703-6094.

Sincerely,

Bob Laux
Director, Technical Accounting and Reporting

Attachment

Issue 1: *Does the IFRS 4 definition of insurance contract identify insurance contracts and sufficiently distinguish those contracts from other financial contracts? Does the GAAP definition of insurance risk identify and separate that risk from other risks such as financial risk? Do the descriptions of finite insurance and reinsurance contracts, including the risk-limiting features, identify those contracts? How could the definitions and descriptions be improved?*

Response: The IFRS 4 definition of insurance contract does identify insurance contracts and, along with the guidance in IFRS 4 of what constitutes significant insurance risk; sufficiently distinguish those contracts from other financial contracts. Unlike U.S. GAAP, this guidance more appropriately defines insurance risk by the nature of the events or occurrences that can trigger a claim and the obligation to compensate for the loss. Microsoft believes this is superior to a mathematical approach based on estimates of future outcomes and we also believe it will obviate the concern that contracts that transfer only limited insurance risk are being accounted for as insurance contracts.

Issue 2: *Can the Statement 113 risk transfer guidance for reinsurance contracts be applied by corporate policyholders and insurers for determining whether an insurance contract transfers significant insurance risk? If not, how can the Statement 113 guidance be modified or clarified to apply to insurance contracts?*

Response: While it is currently being applied by corporate policyholders due to the lack of other guidance, we do not believe it is reasonable to expect the Statement 113 guidance to produce sufficiently credible and accurate risk estimates for a corporate policyholder. The situation of a corporate policyholder is not comparable to that of an insurer, where the insurer may be reinsuring a book of thousands of homogenous insurance policies and the law of large numbers therefore allows a far more accurate risk estimate. Predicting the fortunes of an individual corporate policyholder is akin to asking a life insurance buyer to forecast the time of death of one particular individual.

Issue 3: *Does classifying an entire contract as insurance or bifurcating that contract into insurance and deposit components provide more understandable and decision-useful information? Which qualitative characteristics most influence your decision? Which approach more faithfully represents the economic substance of the contract? Why?*

Response: Microsoft does not believe a requirement to bifurcate insurance contracts will improve financial reporting. Rather, we believe a bifurcation requirement is likely to result in arbitrary allocations and would not result in more representationally faithful financial statements. Furthermore, a requirement to bifurcate would require significant and costly systems changes. However, similar to IFRS 4, we believe that bifurcation is appropriate for insurance contracts containing both an insurance component and a deposit component, provided the deposit component is unambiguously separable as defined by the contract terms.

Issue 4: *The flowchart suggests a sequence for analyzing contracts that integrates current insurance accounting guidance with a hypothetical bifurcation analysis. Do you believe that the sequencing and integration are appropriate? What changes would you propose?*

Response: As indicated above, Microsoft does not believe a requirement to bifurcate insurance contracts will improve financial reporting.

Issue 5: *Do you agree with the characteristics identified for contracts that do or do not unequivocally transfer significant insurance risk? If not, why not? Should other characteristics be added? Are the examples in Appendix B representative of the discussion in paragraphs 57–59?*

Issue 6: *Do you think the characteristics described in paragraph 58 for unequivocal insurance contracts are an improvement over the exemption from cash flow testing in paragraph 11 of Statement 113 (summarized in paragraph 37(c) of this Invitation to Comment)?*

Response: We agree that the examples of insurance contracts in paragraphs 58(a)-(c) fairly represent contracts that typically unequivocally transfer significant insurance risk; however, we note that it is really not possible to arrive at this conclusion with absolute assurance, even in these cases, without assessing the balance of premium to risk transfer.

In addition, Microsoft disagrees with the concept that any loss below the level of expected loss is not real risk transfer, but only "dollar trading", and therefore should be treated as a deposit. As previously indicated, we believe IFRS 4 guidance more appropriately defines insurance risk by the nature of the events or occurrences that can trigger a claim and the obligation to compensate for the loss. For instance, paragraph B18 of IFRS 4 specifically classifies disability and medical coverage as insurance, without regard to whether they are group or individual policies.

Issue 7: *Do you prefer Approach A or Approach B for identifying contracts subject to bifurcation? Why? Do you believe that another approach would be superior? If so, how would you describe that approach? Would your preferred approach be operational? Would it make financial statements more decision useful?*

Response: See our response to Issue 3.

Issue 8: *Should the criteria for bifurcation be different for* ***insurance contracts*** *and* ***reinsurance contracts****? Why? If yes, what differences would you suggest?*

Response: As a corporate policyholder, we do not believe we have the expertise to provide insight on the accounting for reinsurance contracts.

Issue 9: *Which of the methods identified in this Invitation to Comment for bifurcating insurance and reinsurance contracts do you believe has the most conceptual merit? Please explain. Please describe any additional bifurcation methods that you believe should be considered. Would corporate policyholders encounter unique implementation problems in applying any of the methods discussed in this Invitation to Comment?*

Issue 10: *Would data availability limit the development of any of the bifurcation methods discussed in this Invitation to Comment? To what extent are the models that would form the basis for these methods used to underwrite and price products? Would data availability (or lack thereof) affect only certain insurance forms, products, or lines of business? If so, which ones and why?*

Response: See our response to Issue 3.

Issue 11: *In view of the IASB's project on insurance contracts, should the FASB be considering bifurcation of insurance contracts based on transfer of insurance risk?*

Response: Given the IASB's ongoing Insurance Contracts project, Microsoft believes that the FASB should converge with the guidance in IFRS 4.