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Technical Director
Financial Accounting Standards Board
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Submitted via e-mail (director@fasb.org)

Re: File Reference No. 2013-290

Americo Life, Inc. (Americo) appreciates the opportunity to provide comments to the Financial Accounting Standards Board (FASB) on the Insurance Contracts Exposure Draft (the ED).

Americo is a non-public holding company with seven life insurance company subsidiaries which have written or acquired through business combinations or reinsurance transactions life insurance policies and annuity contracts. America's total assets at December 31, 2012 were approximately $6.1 billion. America’s life insurance policies include participating and non-participating whole life, term life, universal life and equity-indexed universal life policies. America's annuity contracts include single premium and flexible premium deferred annuities, immediate annuities, equity-indexed annuities and variable annuity contracts. America prepares consolidated financial statements on the basis of generally accepted accounting principles in the United States (U.S. GAAP). Additionally, each of America's life insurance companies prepares financial statements on the basis of accounting prescribed or permitted by their domiciliary regulator. That basis of accounting follows the principles set forth in the Accounting Practices and Procedures Manual of the National Association of Insurance Commissioners (NAIC STAT).

Our observations in this letter are primarily focused on how the guidance in the ED relates to life insurance products, which for purposes herein are intended to include life insurance and annuity products.

General Comments

We understand the FASB's desire to issue accounting guidance for life insurance which is converged or nearly converged with accounting guidance being proposed by the International Accounting Standards Board (IASB). However, based on the contents of the ED, the desire to reach convergence seems to have been given primary importance ahead of the usual goals of issuing high quality accounting guidance. The expressed objective in the ED is “to increase the decision usefulness of the information about an entity's insurance liabilities, including the nature, amount, timing, and uncertainty of cash flows related to those liabilities, and the effect on the statement of comprehensive income, and to provide comparability, regardless of the type of
entity issuing the contract.” We believe that the guidance in the ED fails many of the aspects of this objective.

Current U.S. GAAP, although not without its flaws and critics, is well-established and generally supportive of the life insurance business models. Furthermore, it is well understood by preparers, analysts, investors and auditors. The FASB has historically made incremental changes to the accounting guidance for life insurance to address concerns of these constituents and to address inconsistencies between accounting guidance for life insurance and general U.S. GAAP guidance. The general theme of the ED seems to be that the life insurance industry is no different from any other industry and that accounting guidance for life insurance needs to be “conformed” to accounting guidance for other industries. The overwhelming complexity of the ED is evidence of the difficulty of this effort. The fact remains that the business of life insurance is fundamentally different from other business types, even other financial services businesses.

The ED contends that the existence of several models for long-duration insurance contracts has led to diversity in practice. The ED also asserts that reducing the number of models for measuring insurance contracts would reduce complexity. We believe that the ED would neither reduce diversity in practice nor reduce complexity. Current U.S. GAAP accounting models seem to recognize the core differences in the business models associated with different insurance products. The ED's solution takes the path of replacing numerous well-understood models with two new models which are not only more complex in their approach, but would be geometrically more difficult to apply in real world situations.

Interestingly, the components of our financial statements which currently create confusion with users are generally those into which the FASB has already introduced fair value concepts which require significant modeling, specifically the accounting for the embedded derivatives associated with equity-indexed annuities.

**Scope**

The definition of insurance contract and, indirectly, reinsurance contract, uses the term “significant insurance risk”. 834-10-55-99 provides further information on the meaning of “significant” as it is applied to “insurance risk”:

Existence of one scenario in which the present value of the cash flows expected to be paid by the entity can significantly exceed the present value of the premiums and other cash inflows will be considered to satisfy the existence of significant insurance risk. That condition can be met even if the insured event is extremely unlikely or even if the expected (that is, probability weighted) present value of the contingent cash flows is a small proportion of the expected present value of all of the remaining cash flows from the insurance contract.

As it applies to life insurance contracts, this definition is largely operable. However, there are at least two types of contracts for which this approach is problematic.
Deferred annuities are issued with annuitization features with guaranteed annuitization purchase rates. Among the annuitization options within a deferred annuity is an option for payments for the remaining life of the annuitant. In practice, annuitization utilization rates are relatively low and the risk of loss from annuitization is minimal.

Under current U.S. GAAP, these contracts are treated as investment contracts in the accumulation phase. A separate liability for the guaranteed annuitization benefits is recorded to the extent that a material liability exists based on expected annuitization rates.

The guaranteed annuitization purchase rates included in a deferred annuity would bring deferred annuities within the scope of the proposed ED guidance. All of the cash flows of a deferred annuity would be subject to the building block approach due to the existence of what might be a de minimis exposure to annuitization losses. An insurance contract liability and an insurance contract margin would then be presented on the statement of financial position. A product that is predominantly an interest spread product would no longer be accounted for or presented as such in the financial statements. The substance of an annuity with a life contingent annuitization feature is much closer to an annuity without such a feature than it is to a life insurance contract.

Our recommendation would be to retain current U.S. GAAP accounting guidance for these products as long as the associated insurance risk is not significant.

Certain reinsurance contracts also contain minimal insurance risk. 834-10-55-17 of the ED includes finite reinsurance contracts among the types of contracts which do not transfer significant insurance risk, although it describes them as follows:

“some finite reinsurance contracts in which the insurer bears limited to no underwriting, credit, investment, and timing risk.”

By the ED’s own definition of insurance risk, it would seem as the “limited” underwriting, credit, investment and timing risk could still constitute significant insurance risk. However, 834-10-55-17 concludes that “The guidance in this topic does not treat those contracts as insurance contracts...”

Section 834-1-55-26-f of the ED includes financial reinsurance contracts that pass all significant insurance risk back to the policyholder as an example of items that are not insurance contracts. However, in almost all financial reinsurance contracts there remains some possibility that the reinsurer will incur losses under the contracts, even if the probability of such losses is remote. Under the ED’s definition of significant insurance risk, financial reinsurance contracts would seem to qualify as insurance contracts.

Under current U.S. GAAP (ASC 944-20-15-60) “a contract that does not subject the reinsurer to the reasonable possibility of significant loss from the events insured by the underlying insurance contracts does not indemnify the ceding entity against insurance risk.” The ED attempts to exclude finite reinsurance contracts and financial reinsurance contracts from its scope, yet the ED’s definition of “significant insurance risk” stands in the way of this attempt. Without additional clarification, the ED could create confusion and diversity in practice.
We would recommend retention of the current U.S. GAAP guidance requiring "the reasonable possibility of significant loss" with regard to determining whether reinsurance contracts need to be accounted for as insurance contracts under the ED.

Although we will not go into a detailed discussion in this letter, we are supportive of the American Bankers Association position that credit risk-related banking products and transactions are fundamentally different from insurance contracts and should be excluded from the scope of the ED.

**Measurement Model**

We are in agreement with the basic premise of the ED that the liability for life insurance contracts should be based on discounted estimated fulfillment cash flows. We also agree that the assumptions used in estimating those fulfillment cash flows should be updated periodically based on available evidence. We are also in agreement that gains should not be recognized upon the issuance of a life insurance contract. However, we strongly believe that the building block approach (BBA) model as proposed in the ED is so conceptually complex that it will create inconsistency between preparers, will not be explicable by management, will reduce investor understanding and be unauditable. Further, the sheer volume of work which would be required to produce financial statements would make it difficult to meet existing financial reporting deadlines.

The BBA requires certain of the measurements to be performed at a portfolio level. The ED definition of a "portfolio of insurance contracts" is vague and could result in more or less groupings than under current U.S. GAAP. We would recommend using the current U.S. GAAP language of grouping insurance contracts "consistent with the entity's manner of acquiring, servicing, and measuring the profitability of its insurance contracts."

We strongly disagree with the use of discount rates based on observable current market prices for the ongoing measurement of the fulfillment cash flows. We understand that the use of discount rates based on current market prices, combined with the ED's proposal to reflect the impact on the liability from changes in such discount rate in other comprehensive income is intended to improve the matching of the assets and liabilities. However, we do not believe that the proposed solution has been proven to eliminate volatility in the financial statements. In fact, the ED solution would seem to move the mismatch between assets and liabilities from other comprehensive income, where it has been readily identifiable, to net income. We would propose using a discount rate based on the entity's portfolio yield measured on an amortized cost basis, reduced for the market risk premium, and the current market yield curve as the basis for estimates of the future investment yields. All changes in the discounted value of the fulfillment cash flows would be reflected in net income. An entity could be required to provide disclosures in the notes to the financial statements to allow readers of the financial statements to understand and evaluate the entity's yield assumptions.
We are concerned about the BBA model's separate measurement and reporting of an explicit margin. Current U.S. GAAP for traditional long-duration insurance contracts includes an implicit margin included as part of the insurance contract liability. Initial measurement of a separate margin might imply a level of precision and place too much significance on the margin. In periods following the initial measurement, the remaining margin becomes nothing more than the initial margin which has been reduced on some basis of recognition. Some respondents to the ED have suggested “unlocking” the margin to offset the effect of changes of assumptions in the calculation of the fulfillment cash flows. Although this suggestion has some conceptual merit, we believe that the amount of historical information which would need to be captured and retained at a portfolio level would make unlocking impracticable in practice. We believe that the current U.S. GAAP approach achieves the most important objectives of recognizing gains from long duration insurance contracts over the life of the contracts rather than at issuance.

We disagree with the treatment of qualifying acquisition costs in the ED as a reduction to the margin. We believe inclusion of qualifying acquisition costs in the fulfillment cash flows would be more conceptually consistent with the other insurance contract costs.

**Reinsurance**

We would recommend that the ED include an illustration of how the reinsurance of an in force block of insurance contracts ceded on a quota share coinsurance basis would be accounted for using the BBA. Such a reinsurance agreement is usually accompanied by an initial transfer of assets from the ceding company to the reinsurer. Although the ceding company is not relieved of its legal obligation to the policyholders, the risks and economic benefits are effectively transferred to the reinsurer. We have some concern that applying the guidance in ED to such a reinsurance transaction will result in accounting which is not consistent with the economics of the transaction. Further, with respect to transition, it would be particularly burdensome and provide no benefit to require an entity to retroactively apply the ED to blocks of insurance contracts which it has ceded through a 100% reinsurance transaction in prior periods.

**Insurance Contract Revenue**

The ED proposes recognition of insurance contract revenue intended to be consistent with principles contained within the FASB's current revenue recognition project. This is another example in which the ED fails to recognize the uniqueness of the life insurance business. The ED is critical of current U.S. GAAP's premium due method. The ED asserts that under the premium due method, an “entity often recognizes insurance contract revenue before the entity has performed the corresponding service, and similarly often recognizes expenses before they have been incurred.” The ED must be asserting that the “service” of a life insurance company consists solely of the payments of death benefits (or other benefits) to policyholders or their beneficiaries. However, we would argue that the service a life insurance company provides is actually taking on the obligation to make payments to the policyholder or beneficiaries. Again, this is a service that is not provided outside of the insurance industry.
In order to fit the BBA model into the structure of the FASB’s general revenue recognition principles, the ED proposes the recognition of insurance contract revenue on an “earned premium” approach. The earned premium approach outlined in the ED is a concept completely new to the life insurance industry which uses the payment of benefits and expenses as the basis for revenue recognition. Under this methodology, an entity would be required to track inception-to-date premiums, benefits and expenses at a portfolio level. When combined with the other aspects of the BBA approach, the combined insurance accounting model becomes extraordinarily complex and would increase data requirements exponentially.

The ED requires that “estimated returnable amounts” (defined as “the estimate of the component of an insurance contract that the entity is required to repay the policyholder or the beneficiary that does not depend on whether an insured event occurs”) be excluded from revenue and expenses and claims. However, these estimated returnable amounts are included in the fulfillment cash flows for purposes of calculating the insurance contract liability. Current U.S. GAAP excludes deposits received and the return of policyholder account balances on universal life-type contracts and annuity contracts. However, this treatment under current U.S. GAAP is consistent with the usage of the account balance as the contract liability. The ED treats the estimated returnable amounts as part of the insurance contract fulfillment cash flows for liability determination purposes but not for revenue or expense purposes.

Beyond our concerns about the theoretical inconsistency discussed above, the ED treatment of returnable cash flows present significant practical difficulties as it would apply to policies both with and without explicit account balances. The ED requires that such returnable amounts be estimated, with such estimates updated each accounting period. This requirement would require the retention of data beyond the current abilities of most life insurance entities.

The ED also proposes to change the recognition of revenues and expenses related to insurance contracts within separate accounts. The ED requires the reporting of gross investment income and offsetting gross investment expense when all investment performance is passed onto the contractholder. This requirement results in an overstatement of revenues and expenses as the insurer is effectively acting as an agent and not a principal in such a transaction. We would recommend retaining the presentation guidance in current U.S. GAAP.

Disclosures

The ED proposes disclosures well in excess of those required under current U.S. GAAP. In fact, the ED disclosure requirements might be in excess of the requirements of any other industry. The volume of information requested as it relates to discount rate, cash flows, inputs, assumptions and risks would be staggering. The sensitivity analysis requirements alone would appear to necessitate an entity maintaining multiple parallel liability calculations, each demanding equivalent data requirements to the entity’s primary liability calculations. While financial statement users may have expressed a desire for this disclosure “wish list”, we cannot
agree that the costs and the information system burdens of this level of disclosure are reasonable in relation to the benefits.

Conclusions

We are deeply concerned by the ED and the magnitude of change it would require and the enormity of the complexity it would introduce. Many of the concepts contained herein appear to have evolved from embedded value disclosures required in Europe. While embedded value disclosures certainly have merit, they should not serve as the basis for a U.S. GAAP insurance accounting model.

The measurements and presentation set forth in the ED will be difficult for preparers to produce and for management to explain to users. We have a real concern whether we would be able to produce financial statements on the basis prescribed in the ED within existing financial reporting deadlines. The volume of the required disclosures seems contrary to the FASB's expressed desire to reduce the current level of disclosures. Further, there would need to be a significant education process for preparers (including the actuarial staff), management and users before any of those groups would be comfortable preparing or using financial statements prepared on the basis of accounting prescribed by the ED. The costs of both the transition and the ongoing application of the guidance currently in the ED would be substantial.

We are not aware of any substantial support for this ED, other than from entities which would benefit from convergence with international financial reporting standards. We have significant interaction with the investment community, and we are not aware of any broad-based support for the accounting models proposed by the ED. Further, we are aware of comments from industry observers that the ED in its current form could make the sector less attractive for investment, thereby reducing the industry's access to capital markets.

We strongly urge the FASB to reconsider the conclusions reached in its Insurance Contracts Projects as such are reflected in the ED. We believe the guidance therein has only been subjected to anecdotal field testing. We believe that comprehensive field testing would shed light on what we believe are real world, practical problems with the measurement and presentation principles contained in the ED. Without a sufficient amount of field testing prior to the issuance of a final standard, we believe the FASB risks moving forward with insurance contracts accounting guidance which could have material adverse consequences on the industry. Ultimately, we would recommend that the FASB reconsider the ED in its present form and focus on targeted improvements to existing U.S. GAAP for insurance contracts.
Thank you for considering our comments.

Sincerely,

Mark Fallon
Senior Vice President and Chief Financial Officer

Donald P. Oster
Vice President and Chief Accounting Officer