Dear Financial Accounting Standards Board:

Protective Life Corporation (the “Company” or “Protective”) appreciates the opportunity to comment on the “Insurance Contracts - Exposure Draft” (“ED”) issued June 27, 2013. Protective operates a group of insurance companies in the United States that market retirement savings, investment, and asset protection products such as life insurance, annuities, guaranteed investment contracts, funding agreements, credit insurance and extended service contracts.

The stated main objective of this standard is to improve, simplify, and enhance the financial reporting requirements for insurance contracts. Further, the FASB aims 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. The FASB seeks to achieve this objective by requiring an entity to measure its insurance contracts under one of two measurement models, referred to as the building block approach and the premium allocation approach. We believe there are aspects of the ED which achieve these main objectives stated by the FASB; however, there are several issues we feel limit the usefulness and appropriateness of the information produced by the proposed standard.

The FASB also seeks to limit the differences between U.S. GAAP and International Financial Reporting Standards (IFRS). Currently, IFRS does not contain a comprehensive standard for insurance accounting, and the International Accounting Standards Board (“IASB”) is in the final stages of a project to issue an insurance accounting standard. Unlike IFRS, U.S. GAAP currently contains comprehensive insurance accounting guidance. The FASB has been working jointly with the IASB with the goal of reaching a converged standard; however, there are significant differences between the IASB revised Exposure Draft and the FASB’s ED. If convergence is not achieved, we strongly believe the significant financial cost, time and effort required for a wholesale change in insurance accounting far outweighs the benefit of a new non-converged standard.

The FASB stated that current insurance accounting under U.S. GAAP has evolved over many years and has resulted in multiple models. The FASB also noted that there are some inconsistencies in accounting for insurance contracts due to current U.S. GAAP accounting guidance that is based on whether an entity providing insurance is an insurance company. We acknowledge the FASB’s assessment of the need for
changes in current U.S. GAAP accounting for insurance contracts, as well as the FASB’s desire to limit differences between U.S. GAAP and a future IASB standard. However, if convergence with IASB is not achieved we believe the FASB should seek targeted changes to current U.S. GAAP in lieu of a comprehensive reconsideration of insurance accounting. Should the FASB decide to shift its focus to targeted changes to current U.S. GAAP, we would be pleased to work with the FASB in identifying and developing the needed changes. Should the FASB decide to move forward with a new comprehensive accounting standard for insurance contracts, as mentioned above, we believe changes are needed to the current proposed Update. We have attached two appendices to this letter which communicate our concerns with the proposed Update and address some of the questions noted in the proposal.

We understand and appreciate the enormity of this project and would be happy to participate in the future as needed. Thank you for the opportunity to comment on the proposed standard. If you have any questions regarding this letter or wish to discuss further, please contact me at (205) 268-6775 or Charles Evers, Vice President, Corporate Accounting (responsible for accounting policy matters) at (205) 268-3596.

Sincerely,

Steven G. Walker  
Senior Vice President, Controller and  
Chief Accounting Officer  
Protective Life Corporation
APPENDIX A - QUESTIONS FOR RESPONDENTS

Scope

Questions for All Respondents

Question 1: Do you agree with the scope and scope exceptions of this proposed guidance, including its applicability to contracts written by noninsurance entities? If not, what types of contracts or transactions also should be included or excluded from the scope and why?

Yes, in general we agree with the scope and scope exceptions of the proposal. Requiring all entities that provide insurance to follow the proposed standard will enhance the comparability of contracts that are identical or similar in nature. The FASB’s proposal requiring an entity to apply one of two models on the basis of characteristics of the insurance contracts is an improvement from current U.S. GAAP. We agree with the FASB that this proposal would minimize the number of models in measuring insurance contracts. We also believe that, with some modifications, this proposal could help reduce existing complexity that has resulted from a product-specific evolution of insurance guidance over the years.

While we understand the FASB’s desire to limit industry specific accounting guidance, in certain situations such guidance is unavoidable. As we state in our response to Question 16, we believe insurers should have an option to elect accounting treatment that avoids asset/liability mismatches without economic substance. We believe the FASB should provide accounting guidance that would best represent the economics of the entity and provide the most useful information to the users of the financial statements.

Recognition

Questions for All Respondents

Question 2: Do you agree with the requirements included in this proposed Update for when noninsurance components of an insurance contract, including embedded derivatives, distinct investment components, and distinct performance obligations to provide goods or services, should be separately accounted for under other applicable Topics? If not, why?

Yes, we agree with the requirements in the proposal to identify and separate noninsurance components of an insurance contract. We also agree with the indicators, listed in 834-10-25-3, that an investment component may not be distinct.

Measurement Approaches

Questions for All Respondents

Question 5: Do you agree that entities should apply different approaches to contracts with different characteristics, described as the building block approach and the premium allocation approach? If not, which model do you think should apply and do you think there should be any changes made to that model?

No, we do not agree. We believe an entity should be given the option to apply either the building block approach (BBA) or the premium allocation approach (PAA) when the application of the two approaches do not result in materially different results. For Protective, we have some multi-year service contracts within our Asset Protection Division that we would like the option of applying the PAA.
Question 6: Do you agree that entities should be required to apply the premium allocation approach if the coverage period of the insurance contract, considering the contract boundary guidance, is one year or less? If not, what would you recommend and why?

No, we do not agree. As stated in our response to Question 5 above, we believe an entity should have the option to use the BBA or PAA when applying the different approaches does not result in materially different results.

Question 7: Do you agree that entities should be required to apply the premium allocation approach if, at contract inception, it is unlikely that during the period before a claim is incurred there will be significant variability in the expected value of the net cash flows required to fulfill the contract? If not, what do you recommend and why?

No, as stated in Questions 5 and 6 above, we believe an entity should have the option to use the BBA or PAA when applying the different approaches does not result in materially different results.

Portfolio and Contract Boundary

Questions for Preparers and Auditors

Question 8: Do you agree with the definition of a portfolio of insurance contracts as included in this proposed Update? If not, what do you recommend and why?

No, we do not agree with the current definition of a portfolio of insurance contracts. The definition as currently drafted would be subject to varying interpretation. The phrases “priced similarly to the risk assumed” and “similar duration and similar expected patterns of release from risk” could result in portfolios at undue level of granularity. For example, these phrases could be interpreted to mean you could not combine identical policies for different age groups as these different age groups could have different profit margins. In Basis of Conclusions (“BC”) 120, the FASB states they rejected requiring portfolios to be comprised by the line of business noting that requirement would result in portfolios at a “fairly granular level”. Based on the basis for conclusions, it seems the FASB does not intend to require overly granular portfolios. Therefore, we suggest updating the portfolio definition to mitigate the concerns noted above. We support the portfolio definition proposed by the American Council of Life Insurers (“ACLI”) in their comment letter to you.

Question 9: Do you agree with the requirements included in this proposed Update on contract boundary (that is, the requirements that establish how to identify the future cash flows that will arise as the insurer fulfills its obligations)? If not, what do you recommend and why?

Yes, we agree with the contract boundary requirements included in this proposal.

Fulfillment Cash Flows

Questions for Preparers and Auditors

Question 10: Do you agree with the types of cash flows that would be included in the measurement of the fulfillment cash flows, including embedded options and guarantees related to the insurance coverage under existing insurance contracts that are not separated and accounted for as embedded derivatives? If not, what cash flows do you think also should be included or excluded and why?

No, we do not agree. We agree with many of the types of cash flows included in the measurement of cash flows; however, we feel the FASB should extend the types of costs that would be included. In the IASB
Revised Exposure Draft, paragraph B66, the IASB states the measurement of the liability includes those cash flows that relate directly to the fulfillment of the portfolio of contracts. The IASB then lists several cash flows that should be considered, including certain costs that can be attributed to the insurance contracts on a reasonable and consistent basis. We feel this IASB definition and listing of cash flows are more representative of the fulfillment cash flows and result in a more accurate insurance contract margin under the building blocks model.

Question 11: Do you agree that the assumptions used in the measurement of the fulfillment cash flows should be updated each reporting period? If not, what do you recommend and why?

No, we do not agree. Based on current guidance found in ASC 944-30-35-7, estimates of expected gross profit used as a basis for amortization are evaluated regularly. We believe the FASB should retain the principle of this guidance and require an entity to consider changes to assumptions used in the measurement of the fulfillment cash flows each reporting period. We also have concerns regarding how these assumption changes should be reflected within the building block model, which we address elsewhere in our letter.

Question 12: Do you agree that the fulfillment cash flows for contracts measured using the building block approach and the liability for incurred claims for contracts measured using the premium allocation approach should be based on an explicit, unbiased, and probability-weighted estimate (that is, the mean) of the future cash flows, as of the reporting date, expected to arise as the entity fulfills the contract, adjusted to reflect any contractual linkage between the contract and any underlying assets? If not, what do you recommend and why?

After taking into account the FASB’s Basis for Conclusions (noted below), we agree the fulfillment cash flows for contracts measured using the building block approach should be based on an explicit, unbiased, and probability-weighted estimate (i.e., the mean) of the future cash flows.

- BC130: “Several respondents to the 2010 FASB Discussion Paper asked for clarification on the expected value measure of cash flows. This was a greater concern for measuring nonlife insurance contracts than life insurance contracts. The Board noted that under existing U.S. GAAP, life insurers perform stochastic modeling for the majority of their products, which includes mortality and lapse rates that are essentially mean rates determined by experience studies (although the models used by life insurers will change to reflect projections for fluctuations in historical rates and should not include adjustments for parameter risks and pandemics). However, nonlife insurers typically record a best estimate liability.”

- BC134: “When considering possible scenarios, an entity need not identify every possible scenario but rather should recognize the statistical mean of possible scenarios that incorporates all relevant information and not simply ignore data or information that is difficult to obtain. In practice, it is not always necessary to develop explicit scenarios if the resulting estimate is consistent with the measurement objective of considering all relevant information in determining the mean.”

- BC134: “Although expected value relies on a range of scenarios that reflect the full range of possible outcomes, the Board decided that practical implementation would depend on actual circumstances. In the Board’s view, enough scenarios should be performed to incorporate all relevant information; if an entity believes it has a sufficient basis to support the mean and performing additional scenarios is not likely to change the mean, an entity does not need to run additional scenarios. Consequently, the Board decided that there should be no requirement to identify and quantify all possible scenarios if the estimate of expected value is unbiased.”

We interpret this guidance to be a principles based approach that would allow the use of multi-scenario stochastic methods or deterministic methods depending on the specifics of each situation, and would allow
certain assumptions to be determined using experience studies. We support this view and believe it will provide reasonable results.

**Questions for All Respondents**

Question 13: Do you agree with the approach in this proposed Update to recognize changes in estimates of cash flows (other than the effect of changes in the liability arising from changes in the discount rates) in net income in the reporting period? If not, what do you recommend and why?

No, we do not agree with the approach in this proposal to recognize changes in estimates of cash flows (other than the effect of changes in the liability arising from changes in the discount rates) in net income in the reporting period. Below we provide our suggestions for how changes in estimates of cash flows should be recognized within the building blocks model, as well as the reasons why.

**Margin** – Within BC197, the FASB states the margin represents the expected profit for an insurance contract at inception. The FASB further lists the “two primary underpinnings” for the margin approach:

a. The entire amount of expected profit (the difference between expected cash inflows and outflows) is at risk.

b. The risk that the actual profit differs from the initial expected profit is due to the uncertainty of the expected cash flows and, therefore, profit should be earned as the uncertainty in the expected cash flows is reduced.

We agree the margin represents the expected profit of a portfolio at inception and we believe the margin should continue to be representative of the profit throughout the life of the underlying insurance contracts. The FASB’s current approach to not adjust the margin for changes in future cash flows results in the following anomalies:

1. **Change in the nature of the margin** - In the current proposal, the margin represents profit at inception and throughout the life of the portfolio assuming there are no future cash flow estimate changes. A portfolio based on an explicit, and unbiased probability-weighted estimate of future cash flows will inevitably have future cash flow changes. Once cash flow changes are noted in a portfolio, the margin no longer represents an expected profit on the portfolio since all future cash flow changes (other than interest rate related changes) are recognized in net income and the margin remains locked. For the margin to start as an amount that represents the expected profit of a portfolio at inception and then no longer represent the portfolio profit after a change in the future cash flow estimate occurs is counterintuitive and could confuse the users of the financial statements.

2. **Recognition of ‘unearned’ profit immediately** – In the current proposal all changes in future cash flow estimates (other than the effect of changes in the liability arising from changes in the discount rates) are recognized in net income immediately. This will result in an entity recognizing the “gain” immediately from favorable future cash flow estimates. This immediate recognition of the “gain” is contrary to the foundational principle of the building blocks model of not recognizing a day one or immediate gain. In addition, whether favorable or unfavorable, the estimate is a future cash flow projection that has not yet occurred. To immediately recognize this estimate, as a gain or loss, in the current period does not represent the true economics of the portfolio.

3. **Windfall gain** – In the current proposal a windfall gain can result when a portfolio becomes onerous. Due to the “locked margin” the remaining unamortized margin would be required to be “unlocked” immediately when a portfolio becomes onerous. This unamortized margin amount will
be written off when unlocked resulting in a windfall gain. In Appendix B, we have included a simple example of a windfall gain that could occur when a portfolio of contracts becomes onerous. For this example the present value ("PV") of future inflows/outflows were used to represent the fulfillment amounts assessed in an onerous contract test.

As you can see in Appendix B, the Locked Margin (Proposed FASB) example results in large swings in profitability (i.e. income statement impact), including a large gain in year 4, the year the portfolio becomes onerous. However, the Unlocked Margin example shows declining profitability of the portfolio beginning in year 2 (year of adverse cash flow estimate development) with a continued downward trend in profitability (income statement impact) in year 3 and a loss recognized in year 4, the year the portfolio becomes onerous. In BC205i, it was noted some FASB members viewed recognizing revenue when the insurer expects greater expected cash outflows as counterintuitive. Although the FASB locked margin approach may address concerns that portfolio revenue could be recognized in a year where adverse cash flow estimates occur, we believe the potential resulting windfall gain if a portfolio becomes onerous is far more concerning. Additionally, as noted above, a locked margin approach would result in an entity recognizing a full impact of a positive cash flow estimate change immediately in net income. This immediate recognition of “profit” that has yet to be “earned” (related to future events) contradicts one of the FASB’s underpinnings of the margin approach.

We believe the FASB should reconsider the locked margin approach, as we believe the unlocked margin approach results in the most economically sound and relevant information for users of the financial statements. We understand there have been some concerns expressed about transparency of insurance accounting in current U.S. GAAP and with an unlocked margin approach. However, we believe the proposed roll forward of reserves disclosures will provide complete transparency for users of financial statements to understand any potential estimate and margin adjustments.

Discount Rates and Discounting

Questions for All Respondents

Question 14: Do you agree that the discount rates used by the entity for nonparticipating contracts should reflect the characteristics of the insurance contract liability and not those of the assets backing that liability? Why or why not?

No, we do not agree. We would prefer for discount rates to be derived from the expected return on actual assets (or a reference portfolio of assets) that are backing, and have similar duration as, the liabilities. This would be consistent with pricing and Asset Liability Management ("ALM") practices employed by insurers and prevent losses (or significantly reduced margin) at inception for contracts that are expected to be profitable overall. This option would more appropriately reflect the economics of the insurance contracts, considering the underwriting and investment ALM functions together.

Question 15: For contracts measured using the premium allocation approach, do you agree that an entity should discount the liability for incurred claims? Do you agree that an entity should be allowed to elect not to discount portfolios when the incurred claims are expected to be paid within one year of the insured event? Why or why not? If not, what would you recommend and why?

Yes, we agree that an entity should discount the liability for incurred claims but be allowed to elect not to discount portfolios when the incurred claims are expected to be paid within one year of the insured event as these amounts would most likely be immaterial.
Question 16: Do you agree that an entity should segregate the effects of underwriting performance from the effects of changes in discount rates (which would reverse over time) by recognizing changes in the present value of the fulfillment cash flows due to changes in the discount rates in other comprehensive income? If not, do you think that the effect of changes in the discount rates should be presented in net income? Please explain your reasoning.

Yes, we agree that an entity should segregate the effects of underwriting performance from the effects of changes in discount rates (which would reverse over time) by recognizing changes in the present value of the fulfillment cash flows due to changes in the discount rates in other comprehensive income. This is a significant improvement from the initial proposal and we strongly urge the FASB to keep discount rate changes within other comprehensive income.

With the decision of the FASB to keep discount rate changes within other comprehensive income, we urge the FASB to also consider a FV-OCI election option - within the Financial Instruments-Overall: Recognition & Measurement project - when measuring assets at FV-OCI would reduce or mitigate an accounting mismatch regardless of the cash flow characteristics or business model. Additionally, we believe an insurer should have an option, at the portfolio level, to elect to present all changes in the liability in net income when doing so would eliminate or mitigate accounting mismatch or appropriately reflect consistent asset-liability management.

Question 17: Because the proposed guidance includes the approach under which changes in the insurance liability arising from changes in the discount rates should be recorded in other comprehensive income, do you think that a test should be required to trigger recognition in net income of some or all of the amounts in accumulated other comprehensive income (that is, a loss recognition test based on asset-liability mismatches)? Why or why not?

No, we do not think a test should be required to trigger recognition in net income of some or all of the amounts in OCI that would reverse over time. In addition, with changes proposed in our response to Question 16, we would not anticipate significant asset-liability mismatches.

Questions for Preparers and Auditors

Question 18: Do you agree that the method for calculating the discount rates should not be prescribed? Is the proposed guidance on determining the discount rates understandable and operable? If not, what do you recommend?

Yes, we agree that the method for calculating the discount rates should not be prescribed. We also believe the proposed guidance on determining the discount rates is understandable and operable. As noted in our response to Question 14 above, we believe discount rates should be derived from the expected return on actual assets backing the liabilities.

Question 19: Do you agree that interest expense generally should be based on the discount rates determined at the date the portfolio of contracts was initially recognized? Why or why not? If not, what do you recommend?

Yes, we agree that interest expense generally should be based on the discount rates determined at the date the portfolio of contracts was initially recognized. Over time, changes in the interest rate and corresponding fluctuations in the liability values will reverse and should be separated from the current period measurement of net income.
Margin for Contracts Measured Using the Building Block Approach

Questions for All Respondents

Question 21: Do you agree that an insurer should not recognize a gain at initial recognition of an insurance contract (such a gain would arise when the expected present value of the cash outflows is less than the expected present value of the cash inflows) but, rather, should defer that amount as profit to be recognized in the future? Why or why not?

Yes, we agree that an insurer should not recognize a gain at initial recognition of an insurance contract (such a gain would arise when the expected present value of the cash outflows is less than the expected present value of the cash inflows). We believe this gain should be deferred and recognized in the future as the entity fulfills the contract.

As stated in Question 13, we believe this gain at inception (i.e. margin) should continue to represent the unearned profit throughout the life of the underlying portfolio of insurance contracts. Therefore, we strongly believe the margin should be "unlocked" for changes in estimates of cash flows (other than interest rate changes). See our response in Question 13 for our detailed discussion around unlocking the margin.

Question 22: Do you support using a one-margin approach, as is included in this proposed guidance, or an explicit risk adjustment and a contractual service margin (as the IASB proposes)? Please explain the reason(s) for your view.

Yes, we support the proposed one-margin approach, as opposed to using an explicit risk adjustment and contractual service margin as the IASB proposes. We agree with the FASB's assessments of the explicit risk adjustment and contractual service margin noted in BC205a and BC205f noted below and feel a one-margin approach is most appropriate.

- BC205a - The risk adjustment and contractual service margin both represent deferred profit. Splitting that deferred profit into two components would be arbitrary.

- BC205f - The risk adjustment and contractual service margin approach is unnecessarily complex relative to the benefits that it would provide.

However, we do support an unlocked margin, similar to the IASB unlocked concept, as noted in our response to Question 13.

Question 23: If you support a risk adjustment and a contractual service margin, do you agree with the IASB's approach to adjust the contractual service margin for changes in estimates of cash flows? Why or why not? Do you agree with the IASB's approach to not specify acceptable approaches to determine the risk adjustment? Why or why not?

As stated in our response to Question 22, we prefer the one-margin approach. However, we do agree with the IASB concept of unlocking the contractual service margin for changes in estimates of cash flows. As stated above, we believe the margin (one-margin approach or the IASB two margin approach) represents deferred profit at inception and should continue to represent profit throughout the life of the underlying insurance contracts.

If the FASB were to adopt the IASB risk adjustment and contractual service margin approach we would agree with not specifying acceptable approaches to determine the risk adjustment. We support a principle based approach as prescribed methods are rarely appropriate in all situations. An entity can disclose the
methodology they used to formulate the risk adjustment to ensure comparability for users of the financial statements.

**Question 24:** Do you agree that a loss at initial recognition of a portfolio of insurance contracts should be recognized immediately in net income (such a loss would arise when the expected present value of the cash outflows exceeds the expected present value of cash inflows)? Why or why not?

Yes, we agree that a loss at initial recognition of a portfolio of insurance contracts should be recognized immediately in net income (such a loss would arise when the expected present value of the cash outflows exceeds the expected present value of cash inflows). This loss recognition would be consistent with the general loss recognition criteria utilized through current U.S. GAAP.

**Questions for Preparers and Auditors**

**Question 25:** Do you agree with the proposed method(s) of recognizing the margin (that is, as the entity is released from risk under the insurance contracts as evidenced by a reduction in the variability of cash outflows)? If not, what do you suggest and why?

In general yes, we agree with the proposed method(s) of recognizing the margin (that is, as the entity is released from risk under the insurance contracts as evidenced by a reduction in the variability of cash outflows). This principles based approach will provide the opportunity for an entity to properly recognize an amortization basis that is consistent with the release of risk concept to the various insurance contract products which have unique risk patterns. We do urge the FASB to unlock the margin as detailed in our response to Question 13.

**Question 26:** Do you agree that interest should be accreted on the margin and therefore affect insurance contract revenue? If not, why?

Yes, we agree that interest should be accreted on the margin. We believe the accretion rate(s) for the margin should be the same as the accretion rate(s) used for recognition in the income statement on the unwinding of the discounted cash flows.

**Question 27:** Do you agree that if the expected cash outflows (including qualifying acquisition costs) of a portfolio of insurance contracts will exceed the expected cash inflows, an entity should recognize the remaining margin immediately in net income? Why or why not?

No, we do not agree. We urge the FASB to adopt an unlocked margin approach. Without an unlocked margin approach, an entity could recognize a gain when a portfolio of insurance contracts becomes onerous (i.e. windfall gain). See our illustration of a windfall gain in our response to Question 13. If the FASB were to adopt an unlocked margin approach, the margin would be adjusted for estimated future cash flow changes and be representative of profit throughout the life of the underlying insurance contracts. The remaining margin would still need to be written off in the event the expected cash outflows (including qualifying acquisition costs) of a portfolio of insurance contracts exceed the expected cash inflows within an unlocked model; however, there would not be a resulting windfall gain as seen in our windfall gain illustration. In addition, we believe an unlocked margin approach results in a better representation of the economics of a portfolio of insurance contracts and reduces the burden of assessing an onerous contract (or loss recognition test) by not requiring an entity to track a locked margin.

**Acquisition Costs**

**Questions for Preparers and Auditors**
Question 28: Do you agree that the direct acquisition costs presented with the margin should include only the costs directly related to the entity’s selling efforts that result in obtaining the contracts in the portfolio and that all other acquisition costs should be recognized as expenses when incurred? If not, what do you recommend and why?

No, we do not agree that the direct acquisition costs presented with the margin should include only the costs directly related to the entity’s selling efforts that result in obtaining the contracts in the portfolio and that all other acquisition costs should be recognized as expenses when incurred. We support the IASB view that all related acquisition costs should be treated as fulfillment cash flows because acquisition costs associated with unsuccessful efforts are costs incurred to acquire a portfolio of insurance contracts and are factored into the expected profits of the portfolio. Therefore, in order to ensure the margin reflects expected profits, acquisition costs associated with unsuccessful contract efforts need to be included as cash outflows.

Question 29: Do you agree that the measurement of the margin for contracts measured using the building block approach and the liability for remaining coverage for contracts measured using the premium allocation approach should be reduced for direct acquisition costs incurred? If not, what do you recommend?

No, as noted in our response to Question 28, we believe acquisition costs (both successful and unsuccessful) should be treated like any other cash outflow in determining the margin. Requiring a segregation of acquisition costs to reduce the margin adds complexity to both measurement and presentation, with no benefit to the users of the financial statements.

Question 30: Do you agree that an entity should recognize acquisition costs as an expense in net income in the same pattern that it recognizes the margin for contracts measured using the building block approach or in the same pattern that it reduces the liability for remaining coverage under the premium allocation approach? If not, why not?

No, we do not agree. At stated above, we believe acquisition costs are part of the fulfillment cash flows and should be treated similar to other cash outflows when determining the margin.

Insurance Contract Revenue

Questions for All Respondents

Question 31: Do you agree that users of financial statements would obtain relevant information that faithfully represents the entity’s financial position and performance if, in net income, for all insurance contracts, an entity presents insurance contract revenue and incurred expenses, rather than only information about changes in margins (that is, the net profit)? If not, why not?

We agree in part; however, we feel significant changes are needed. The insurance revenue model as proposed by the FASB, known as the earned premium approach, is a divergence from the FASB’s summarized margin approach as proposed in the 2010 FASB Discussion Paper and results in a complex calculation that produces less relevant information for financial statement users. Within BC290, the FASB noted one consequence of the original summarized margin presentation is that information about premiums, claims, and expenses for the period would not be presented in the statement of comprehensive income. Although we agree with the FASB’s reasoning that more information is needed on the statement of comprehensive income other than just the summarized margin, we feel the earned premium approach is not an improved model and should be modified. We believe the margin is a key indicator of insurance performance and should be explicitly presented in the statement of comprehensive income. The FASB should adopt an approach that both explicitly presents the margin, as well as information about premiums, claims, and expenses in the statement of comprehensive income. We support the Building Block Elements
approach proposed by the ACLI in their comment letter, which we feel achieves the goal of explicitly presenting the margin as well as information about premiums, claims and expenses in the statement of comprehensive income.

Question 32: Do you agree that, for all contracts, revenue should exclude any amounts received that an entity is obligated to pay to policyholders or their beneficiaries regardless of whether an insured event occurs and that expenses should exclude the corresponding repayment of those amounts? If not, what do you recommend? Please specify whether your view depends on the type of contract.

No, we do not agree that revenue should exclude any amounts received that an entity is obligated to pay to policyholders or their beneficiaries regardless of whether an insured event occurs and that expenses should exclude corresponding repayment of these amounts. We believe the estimated returnable amounts should be included in the reporting of premiums and expenses in the statement of comprehensive income. Separating interrelated cash flows and excluding them from the insurance contract revenue/incurred expenses is too complex and does not provide more useful information to the users of the financial statements.

Questions for Preparers and Auditors

Question 34: For contracts measured using the building block approach, does this proposed Update contain sufficient guidance on how to determine insurance contract revenue in accordance with the principle that it should be allocated between reporting periods as performance obligations are satisfied over time (that is, to allocate consideration between periods by reference to the relative value of the services provided in each period)? If not, explain what additional guidance is necessary.

Yes, for contracts measured using the building block approach, we agree the proposed Update contains sufficient guidance on how to determine insurance contract revenue in accordance with the principle that it should be allocated between reporting periods as performance obligations are satisfied over time (i.e., allocate consideration between periods by reference to the relative value of the services provided in each period). As discussed in our response to Question 31, we do not support the earned premium approach and suggest a modification to the presentation of revenue.

Participating Contracts

Questions for Preparers and Auditors

Question 35: Do you agree that participation features that are contractually dependent on the performance of other assets or liabilities of the insurer or the performance of the entity itself should be measured on the same basis used to measure the underlying items and changes in the measurement should be presented in the same statements (that is, net income or other comprehensive income)? Do you agree that this approach should be limited to only participating features for which the amount of the performance of the underlying items passed through to policyholders is contractually determined and not extended to participating features that allow an entity discretion about the amount of the performance of the underlying item to pass through to the policyholders? If not, what do you recommend and why?

Yes, we agree that participation features that are contractually dependent on the performance of other assets or liabilities of the insurer or the performance of the entity itself should be measured on the same basis used to measure the underlying items and changes in the measurement should be presented in the same statements (that is, net income or other comprehensive income). We also agree this approach should be limited to participating features for which the amount of the performance of the underlying items passed through policyholders is contractually determined and not extended to participation features that allow an entity discretion about the amount of the performance of the underlying item to pass through to the policyholder.
Reinsurance

Questions for All Respondents

Question 36: Do you agree that a cedant should record a margin if the expected present value of the cedant’s future cash inflows exceed the expected present value of the cedant’s future cash outflows (thus prohibiting the recognition of a gain at inception upon entering into a reinsurance arrangement) for (a) retrospective reinsurance contracts accounted for using either the building block approach or the premium allocation approach and (b) prospective reinsurance contracts accounted for using the building block approach? If not, what do you recommend and why?

Yes, we agree with both (a) and (b).

Questions for Preparers and Auditors

Question 37: Do you agree that a cedant should estimate the fulfillment cash flows (including the ceded premium) for a reinsurance contract using assumptions consistent with those used to measure the corresponding fulfillment cash flows for the underlying insurance contract or contracts, without reference to the margin on the underlying contracts? If not, what would you recommend and why?

Yes, we agree.

Insurance Contracts Acquired in a Business Combination

Questions for All Respondents

Question 38: Do you agree that entities should record a loss at the acquisition date in the amount by which any excess of the asset and liability balances related to insurance contracts measured in accordance with the guidance in this proposed Update exceeds the fair value of those assets and liabilities? Do you agree that entities should record a margin (not an immediate gain) for the amount that the fair value of the asset and liability balances exceeds those assets and liabilities measured in accordance with the guidance in this proposed Update? If not, do you think an entity should instead increase or decrease goodwill for the differences between the fair value and the measurement in accordance with the guidance in this proposed Update on those assets and liabilities? Why or why not?

No, we do not agree. We agree that entities should record a margin (not an immediate gain) for the amount that the fair value of the asset and liability balances exceeds those assets and liabilities measured in accordance with the guidance in this proposed Update. However, we do not agree an entity should record a loss at the acquisition date in the amount by which any excess of the asset and liability balances related to insurance contracts measured in accordance with the guidance in this proposed Update exceeds the fair value of those assets and liabilities. We believe the FASB should consider adopting the proposed IASB approach which would be to adjust goodwill in situations where the present value of fulfillment cash flows exceeds the fair value of the insurance contract liability.

Contract Modifications

Questions for Preparers and Auditors

Question 39: Do you agree that for a substantial modification (a) an entity should recognize a gain or loss as the difference between the measurement of the modified contract using the current entity-specific price that the entity would hypothetically charge the policyholder for a contract equivalent to
the new contract and the carrying amount of the existing contract and (b) that the carrying amount of the existing contract should be derecognized? If not, what do you recommend?

No, we do not agree. We strongly urge the FASB to unlock the margin as discussed in our response to Question #13 and elsewhere in our letter. We believe unlocking the margin would significantly reduce the complexity of the contract modification assessment. If the FASB decides to unlock the margin, we believe the IASB’s approach to the modification and derecognition of an insurance contract as detailed in paragraph 49 of the IASB revised ED is an effective assessment approach.

Presentation

Questions for All Respondents

Question 40: Do you agree with the presentation requirements included in this proposed Update? If not, what would you recommend and why?

No, we do not agree with the presentation requirements included in this proposed Update. We have several issues with the current requirements, as noted below:

- **Earned premium approach for insurance revenue** – We have significant concerns with the current earned premium approach proposed by the FASB. We do not feel this presentation will provide users with relevant and useful information. See our response in Question 31 for more details.

- **Estimated returnable amounts** – As discussed in our response to Question 32, we believe estimated returnable amounts should be included in the reporting of premiums and expenses in the statement of comprehensive income.

- **Separation of insurance (and reinsurance) contracts that are in an asset and liability position** – The FASB should propose net presentation of the insurance (and reinsurance) contracts in the face of the Statement of Financial Position. Entities should then separate and present portfolios in an asset or liability position separately in the footnotes to the financials.

- **Netting of separate account income and expenses** – We believe the FASB should retain current U.S. GAAP under which separate account income and expenses are netted. The proposed Update requires an entity to present investment income generated from the assets in the qualifying segregated fund arrangements and the interests credited to policyholders as a pass through of that investment income and interest expense, respectively, in net income.

Disclosure

Questions for All Respondents

Question 41: Do you agree with the disclosure requirements included in this proposed Update? If not, which disclosure requirement(s) would you change and why? Are there any additional disclosures that would provide decision-useful information and why? Do you think that any of the disclosure requirements included in this proposed Update would not provide decision-useful information and should not be required? If so, which ones and why?

No, we do not agree with the disclosure requirements included in this proposed Update. As currently proposed, we feel the disclosures are overly burdensome for preparers and will overwhelm the users of the financial statements. We understand the need to provide disclosures that help users understand the amounts reported in the financial statements and the estimations involved; however, we feel the proposed disclosures
are too granular and cause significant concerns for preparers, users, and auditors. As discussed in our previous letter to the FASB regarding Disclosures about Liquidity and Interest Rate Risk dated September 25, 2012, we feel the level of detail required in disclosing inputs, judgments, and forward looking assumptions would be more appropriately disclosed in the Management Discussion and Analysis (MD&A) section of the Annual Report on Form 10-K. This would allow preparers more freedom to appropriately discuss management judgments and other key looking forward assumptions in an MD&A discussion protected by certain Safe Harbor Rules. In addition, it may be impractical to require that such data be covered by the criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

Effective Date and Transition

Questions for Preparers and Auditors

Question 42: The Board will establish the effective date of the requirements when it issues the final amendments. However, the Board is interested in determining the key drivers affecting the timing of implementation. What are those key drivers? How do those drivers affect the time it will take to implement this proposed guidance?

The proposed Update is a complete overhaul of insurance accounting and will take significant time and effort to implement. Some of the key drivers affecting the timing of the implementation are listed below:

- **Impacts on Systems and Processes**
  - Establishing processes to identify scope and classifications of our products
  - Assess whether we currently have appropriate models and tools necessary to handle the new proposed Update requirements (i.e. modeling capabilities, data requirements, interfaces and mapping, capacity and run times)
  - Systematically adjust discount rates at each reporting period while tracking original discount rates for OCI determination
  - Designing and implementing a system to track the margin and its release
  - Designing internal controls over the new processes
  - Updating systems and processes for new reporting requirements

- **Impacts on Employees and Stakeholders**
  - Implement training for finance, actuarial, IT, underwriting, and risk management
  - Add incremental resources as needed
  - Communicate changes to stakeholders to understand new metrics and performance results.
  - Assess the impact on key performance indicators
  - Assess the impact on investment allocation and asset-liability management
  - Manage and communicate the various implementation needs of the proposed Update, all of which divert an entity’s time and resources away from the core business plan

- **Transition Impacts**
  - Manage dual reporting during the changeover process
  - Assess additional resource requirements, specifically in modeling and actuarial processes
  - Develop information needed for full retrospective application of the standard, as well as compile financial information needed for the Securities and Exchange Commission’s five year disclosure requirement
  - Incorporate the impact of the proposed Update on other significant proposed Accounting Standard Updates (i.e. Financial Instruments, Revenue Recognition, Leases, etc.)
  - Develop implementation plans for the proposed Update, while addressing evolving Statutory and other Regulatory requirements
Each of the three drivers listed above, among others not listed, will result in a tremendous amount of time and effort. Sufficient lead time is needed from the time a final standard is issued to the effective date to allow companies to address the multiple changes that will need to be implemented. Due to the key drivers listed above as well as other items that will be identified, we would encourage the FASB to allow four years of lead time. We also encourage the FASB to coincide the implementation of the Financial Instruments Standards with the Insurance Contracts Standard to allow insurers and other impacted companies to have an appropriate amount of time and opportunity to assess the full impact of these interrelated projects.

**Question 44:** Do you agree that the practical expedients relating to transition included in this proposed guidance are sufficient for retrospective application (that is, are the transition provisions in this proposed guidance operable)? If not, what would you recommend and why?

No, we do not agree. We appreciate and agree with the practical expedients relating to transition included in this proposed guidance; however, we still feel it will be a challenge to implement some aspects of a full retrospective application without the benefit of hindsight. Some issues that present a challenge are performing the following from inception to the transition date for every portfolio, or portion of the portfolio:

- an assessment and accounting for all substantial and non-substantial contract modifications,
- amortization of margin,
- onerous contract test to ensure the margin should not have been released at any point in the life of the contracts, among others.

We strongly encouraged the FASB to consider allowing preparers the option to use the practical expedient provided in the proposed IASB standard, as outlined in paragraphs C5 and C6, which allows the ability to use the benefit of hindsight in determining the cash flows necessary to determine the margin at transition. Allowing a hindsight approach will mitigate the operational concerns noted above and provide a reasonable representation of the margin at transition.

**Question 45:** For business combinations that occurred before the transition date, is the requirement included in this proposed Update on reallocating the fair value of the asset and liability balances related to insurance contracts between the expected fulfillment cash flows and the margin operable? Why or why not? If not, what would you recommend and why?

No. We agree that entities should record a margin for the amount that the fair value of the asset and liability balances exceeds those assets and liabilities measured in accordance with the guidance in this proposed Update. However, we do not agree an entity should record a loss in the amount by which the excess of the asset and liability balances related to insurance contracts measured in accordance with the guidance in this proposed Update exceeds the fair value of those assets and liabilities. We believe the FASB should consider adopting the proposed IASB approach which would be to adjust goodwill in situations where the present value of fulfillment cash flows exceeds the fair value of the insurance contract liability.

**Questions for Users and Auditors**

**Question 46:** Do you agree that the proposed approach to transition would provide users of financial statements with relevant information that faithfully represents the entity’s financial position and performance in a way that appropriately balances comparability with verifiability? Why or why not?

Yes, we agree that the proposed approach to transition would provide users of financial statements with relevant information that faithfully represents the entity’s financial position and performance in a way that appropriately balances comparability with verifiability. In the 2010 IASB Exposure Draft, the IASB proposed that an entity should, on first applying the proposed guidance, measure its existing contracts at that
date by setting the contractual service margin to zero. As noted in BC404, both the IASB and FASB received comment letters criticizing this approach due to the lack of comparability between contracts that were in force at the date of transition and those that would be initially recognized after the date of transition. The largest concern, as noted, was the inconsistency in the earnings for contracts written before and after the transition date. This lack of comparability and consistency would have a lasting impact due to the long duration of insurance contracts. We completely agree with these points and strongly agree that entities should apply the transition fully retrospectively. We believe the cost and burden associated with a fully retrospective application of the proposed model are justified and will result in the most comparable and relevant information to the financial statement users.

We also agree with the FASB’s decision discussed in BC408. When full retrospective application of the proposed model would not be practicable, entities would be allowed to recognize an estimate for the margin on portfolios of contracts written before the earliest period practicable to apply the proposed model retrospectively. Further the FASB decided to allow insurers to determine the earliest practicable date that the guidance in the proposed Update can be applied retrospectively by portfolio of contracts as opposed to requiring all entities to use a consistent date across all of its portfolios. In BC412, the FASB acknowledged that historical data will most likely have been accumulated based on the existing definition of a portfolio and some entities’ portfolios may potentially change groupings as a result of the proposed guidance. Therefore, the FASB determined contracts written before the transition date may be grouped into separate portfolios from contracts written or substantially modified after the transition date if the entity’s determination of the portfolio differs from what the portfolio would be under the proposed guidance. We feel these decisions provide companies the flexibility needed to produce comparable and relevant transition information.

We also encourage the FASB to incorporate the additional practical expedient as detailed in our response to Question 44.

**Costs and Complexities**

**Questions for Preparers**

**Question 47:** Describe the nature of the incremental costs of adopting the guidance in this proposed Update, distinguishing between one-time costs and ongoing costs. Explain which aspects of the guidance in this proposed Update are driving those costs and include ideas to make the proposal more cost effective.

In our response to Question 42 above, we noted several key drivers that affect the timing of the implementation. These same drivers result in a significant amount of incremental and ongoing costs.

Significant one-time costs will be incurred, as noted below:
- Actuarial and financial reporting system upgrades to ensure we have the appropriate models and tools to handle the proposed Update
- Implement training for finance, actuarial, IT, underwriting, and risk management areas
- Related to transition, costs related to managing dual reporting during the changeover process as well as costs related to the research and accumulation of data necessary for retrospective adoption

There will also be ongoing costs associated with the adoption of the proposed Update including:
- Increased employment resources
- Increased audit fees
- Ongoing training and communication to investors
- Continued research of the impact of the proposed Update on current and future product offerings
- How the Proposed Update will have an impact on the constantly changing regulatory environment
We believe several key issues noted in our letter (e.g. locked in margin) would add complexity to the standard and increase cost significantly. Also noted in our letter, we strongly believe if convergence is not achieved, the significant financial cost, time and effort required for a wholesale change in insurance accounting far outweighs the benefit of a new non-converged standard. Additionally, we acknowledge the FASB's assessment of the need for changes in current U.S. GAAP accounting for insurance contracts, as well as the FASB's desire to limit differences between U.S. GAAP and a future IFRS standard. However, we believe the FASB should seek targeted changes to current U.S. GAAP in lieu of a comprehensive reconsideration of insurance accounting.
APPENDIX B – Windfall Gain Example

Windfall gain example
• 10 year level term portfolio
• Outflow and ‘release of risk’ margin run off on a straight line pattern
• The “additional outflow” column represents the adverse future cash flow assumption changes
• The future cash flow changes are expected to occur later in the contract (year 5 or later)
• The portfolio becomes onerous in year 4
• The windfall gain is seen in the Proposed FASB table below in year 4
• Note, all PV amounts are assumed to be discounted at the inception (year 0) discount rate

<table>
<thead>
<tr>
<th>Year</th>
<th>PV Inflow</th>
<th>PV Outflow</th>
<th>Additional PV Outflow</th>
<th>Total PV Outflow</th>
<th>Margin Liability</th>
<th>I.C. Liability</th>
<th>I/S Impact</th>
</tr>
</thead>
<tbody>
<tr>
<td>0</td>
<td>$1,000</td>
<td>$800</td>
<td>$0</td>
<td>$800</td>
<td>$200</td>
<td>($200)</td>
<td>$0</td>
</tr>
<tr>
<td>1</td>
<td>$900</td>
<td>$720</td>
<td>$0</td>
<td>$720</td>
<td>$180</td>
<td>($180)</td>
<td>$20</td>
</tr>
<tr>
<td>2</td>
<td>$800</td>
<td>$640</td>
<td>$100</td>
<td>$740</td>
<td>$160</td>
<td>($60)</td>
<td>($80)</td>
</tr>
<tr>
<td>3</td>
<td>$700</td>
<td>$660</td>
<td>$20</td>
<td>$680</td>
<td>$140</td>
<td>($20)</td>
<td>$0</td>
</tr>
<tr>
<td>4</td>
<td>$600</td>
<td>$600</td>
<td>$90</td>
<td>$690</td>
<td>$0</td>
<td>$90</td>
<td>$50</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Sum ($10)</td>
<td></td>
</tr>
</tbody>
</table>

With Locked Margin (Proposed FASB)

<table>
<thead>
<tr>
<th>Year</th>
<th>PV Inflow</th>
<th>PV Outflow</th>
<th>Additional PV Outflow</th>
<th>Total PV Outflow</th>
<th>Margin Liability</th>
<th>I.C. Liability</th>
<th>I/S Impact</th>
</tr>
</thead>
<tbody>
<tr>
<td>0</td>
<td>$1,000</td>
<td>$800</td>
<td>$0</td>
<td>$800</td>
<td>$200</td>
<td>($200)</td>
<td>$0</td>
</tr>
<tr>
<td>1</td>
<td>$900</td>
<td>$720</td>
<td>$0</td>
<td>$720</td>
<td>$180</td>
<td>($180)</td>
<td>$20</td>
</tr>
<tr>
<td>2</td>
<td>$800</td>
<td>$640</td>
<td>$100</td>
<td>$740</td>
<td>$160</td>
<td>($60)</td>
<td>($80)</td>
</tr>
<tr>
<td>3</td>
<td>$700</td>
<td>$660</td>
<td>$20</td>
<td>$680</td>
<td>$140</td>
<td>($20)</td>
<td>$0</td>
</tr>
<tr>
<td>4</td>
<td>$600</td>
<td>$600</td>
<td>$90</td>
<td>$690</td>
<td>$0</td>
<td>$90</td>
<td>($45)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Sum ($10)</td>
<td></td>
</tr>
</tbody>
</table>