October 25, 2013

Technical Director
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

RE: Insurance Contracts (Topic 834) (File Reference 2013-290)

Genworth Financial, Inc. (“Genworth”) appreciates the opportunity to comment on the Financial Accounting Standards Board’s (the “Board” or “FASB”) Exposure Draft on Insurance Contracts (the “Proposal” or “ED”).

Genworth is a leading financial services company dedicated to providing insurance, investment, and financial solutions to more than 15 million customers, with a presence in more than 25 countries. We are a multi-line insurer and offer a variety of insurance products, including life, long-term care, mortgage guaranty, annuities, and payment protection coverages.

We support the Board’s objective to improve U.S. generally accepted accounting principles (“GAAP”) for insurance contracts by developing high-quality guidance through improving, simplifying, and achieving convergence of the financial reporting requirements for insurance contracts, and to provide investors with decision-useful information. We have reviewed and evaluated the Proposal and concluded that the guidance, if adopted, would not achieve these goals.

In fact, if adopted, the Proposal would have a significant, unfavorable impact on the industry and our company. This conclusion is grounded on the additional complexities, artificial volatility, reduced clarity and comparability, and the clouding of decision-useful information the Proposal would introduce. The elimination of long-standing valuation and performance metrics increases our concern that investors and analysts would fail to find incremental benefit that would exceed the impact to our earnings and investment value from the significant implementation and ongoing operational costs. Additionally, the Proposal would result in financial statements that would not reflect how we manage our businesses or evaluate performance, both of which are instrumental in providing users decision-useful information. Insurers manage risk based on cash flows where temporary or short-term changes in behavior or market assumptions are irrelevant to contracts that are fixed and/or long term in nature. However, the proposed measurement approach would capture these temporary or short-term changes in the financial statements and would present information that is inconsistent with how we manage these risks.

Overall Concerns & Recommendation

Although we appreciate the Board’s efforts, Genworth respectfully and fundamentally disagrees with the proposed guidance. We acknowledge some improvements are needed to simplify and
eliminate certain complexities and inconsistencies in existing U.S. GAAP; however, the foundational measurement and reporting within current guidance serves investors well today and therefore must be preserved.

The proposed building blocks measurement model, which results in a comprehensive change in the measurement and reporting for insurance contracts, is unwarranted and would add significant additional complexity to a business that is already difficult to understand. A more appropriate approach would be to focus on targeted improvements to existing, established, and well-understood guidance. The Proposal’s single measurement model for all long-duration products exponentially increases complexity, results in additional costs, reduced clarity and incomparability of companies, and compromises the decision usefulness of the financial statements.

We have modeled the Proposal on many of our insurance contracts. This modeling exercise raises numerous practical implementation difficulties and, in almost all cases, produces profit patterns that are vastly different, more volatile, and in many cases, economically illogical. While we realize accounting impacts the pattern of earnings recognition over the life of an insurance contract, but not the ultimate result, the patterns identified through our modeling, if unchanged in the final standard, will inevitably have an impact on the availability and pricing of our insurance contracts. Practical considerations and detailed modeling of a new standard in a variety of circumstances should be part of the FASB’s process prior to issuing final guidance. We also urge the Board to undertake more robust inquiry of equity analysts and other users of financial statements to evaluate the usefulness of the Proposal.

Today, investors use our consolidated U.S. GAAP financial statements as the primary tool for evaluating our current and future potential earnings, with secondary emphasis on our statutory financial statements in order to obtain a comprehensive view of our financial condition. Any changes to the accounting for insurance contracts that are adopted must continue to allow us to provide accurate, meaningful information to investors, analysts, and other users of our financial statements. If the Proposal is adopted, our financial statements will not accurately reflect the long term nature of our insurance contracts (some as long as forty years or more), how we manage our business, nor how users of our financial statements evaluate our businesses. As a result, we would be forced to use non-GAAP measures as the primary method of explaining our business results and evaluating our performance, potentially reducing the preparation of U.S. GAAP financial statements to a compliance exercise. Any increased focus on non-GAAP measures would further diminish comparability and reliability, as these measures would likely not be subject to audit or the same level of controls that accompany the key metrics utilized today (that are primarily based on information obtained from financial statements).

Further, investors would also place increased reliance on our statutory financial statements for evaluating operating performance, a function for which they are ill-suited, as these financial statements are necessarily focused on solvency and claims-paying ability. The Proposal also moves current U.S. GAAP further away from the statutory accounting model that is used by insurers to manage themselves from a regulatory, capital and dividend viewpoint, creating further confusion for investors that use both U.S. GAAP and statutory financial statements.

The insurance industry’s ability to attract and retain capital is heavily dependent upon investor appetite and confidence, both of which are fueled by access to decision-useful information in
financial statements. The Proposal has the potential to disrupt the insurance industry’s ability to obtain capital as well as impact certain financial markets supported heavily by insurance businesses. The significant non-economic volatility created by the Proposal would likely increase the cost of capital for insurers, which could have the unintended consequence of forcing them to raise prices, issue shorter-duration products or even exit certain businesses. These consequences are particularly relevant for longer-term contracts such as permanent life insurance and long-term care insurance. Additionally, insurers are significant providers of long term financing to governments, municipalities, and corporations that help support the consumer financial and housing markets and protect individuals’ financial security. Adverse impacts on long-duration insurance products could reduce the attractiveness of longer-term investments for insurers, thereby reducing the ability of investees to obtain financing from the insurance sector or increasing the cost of this financing.

Convergence with International Financial Reporting Standards (“IFRS”), not user concerns with existing guidance, prompted the Board to evaluate wholesale changes to insurance contracts accounting. IFRS lacks comprehensive accounting principles for insurance contracts; on the other hand, the FASB has robust, comprehensive, and well understood principles and guidance in place today. To move toward the IFRS approach in the absence of complete convergence would result in undue costs, burden, and significant incremental complexity on stakeholders that currently utilize U.S. GAAP financial statements for insurance companies. Accordingly, we believe a significantly higher burden exists for making wholesale changes to U.S. stakeholders, further supporting our view that an approach starting with the well-accepted current U.S. GAAP and making targeted improvements is more appropriate and would adequately address those improvements that are deemed necessary.

The existing principles included in current U.S. GAAP were developed over a number of years in response to new products. While multiple measurement models may be criticized as increasing complexity, we believe an approach of making targeted changes to U.S. GAAP that leverages existing guidance would provide a far superior starting point and would promote the prominent display of decision-useful information on the face of the financial statements.

Primary Issues with Proposal

We have included our specific observations on the issues with the Proposal within our responses to the Questions For Respondents (see Appendix). The various aspects of the model where we have significant concerns include:

- Locked In Margin
- Discount Rate That Disregards Asset/Liability Matching
- Disaggregation Resulting from the Portfolio Definition
- Significant Complexity & Change For Account Value Products
- Income Statement Presentation
- Voluminous & Onerous Disclosures
- Application Of Building Blocks Approach To Mortgage Guarantee Insurance

As noted in our responses to the questions, the Proposal would result in a significant increase in complexity, not only for preparers (to determine how to apply the proposed guidance), but also for users (to understand, compare, and analyze the performance of insurance companies). If we were required to adopt the Proposal as currently written, we anticipate the internal costs for us to
implement the proposed guidance would be in excess of $100 million from significant additional resources and enhancements in systems and capabilities to produce the necessary information required under the proposal. For ongoing costs, we anticipate the incremental internal costs to be in excess of $25 million annually as a result of increased financial reporting, actuarial, and system costs. These estimates of implementation and ongoing costs excludes any additional fees to be paid to audit firms or external consultants, which could be sizable.

Please see Appendix for our responses to the questions included in the proposal where we provide additional perspective on the technical application of the model and additional support for the Board limiting any proposed changes to targeted improvements in existing U.S. GAAP.

**Targeted Improvements to U.S. GAAP**

If the Board focused on targeted improvements to U.S. GAAP, it could achieve all its objectives except for convergence (which the Proposal would not achieve anyway), while preserving the relevance of historical U.S. GAAP financial results. We have included a listing of targeted improvements that could be considered by the Board:

- **Locked-In Assumptions For Long Duration Contracts (Traditional Products)** – We believe the Board should eliminate the use of locked-in assumptions for these products. Dynamic assumptions would allow investors and analysts to have constant, real time insight into management’s expectations of future performance. Using targeted improvements to allow for updating of assumptions utilizing the existing aggregation and discount rate guidance would avoid many non-beneficial system changes and significant, unfavorable impacts that would result from applying the Proposal.

- **DAC Amortization** – Corresponding with a change in locked-in assumptions for Traditional products, we believe the DAC amortization guidance could be simplified and made consistent for all products. We recognize that there are critiques of the existing DAC amortization guidance, which results in volatility from updating assumptions for Non-traditional products. Such amortization could be prospectively applied to changes in assumptions, rather than updating the amortization each period based on more of a retrospective (actual vs. expected) method that can cause DAC amortization adjustments to be both positive and negative.

- **Mortgage Insurance Premium Recognition** – Mortgage insurance is scoped out of most aspects of existing insurance and financial guarantee accounting guidance. Industry practice and U.S. GAAP have developed primarily based on National Association of Insurance Commissioners statutory guidance that primarily follows a short duration accounting model. We believe prescriptive guidance, similar to today’s industry practices should be written into U.S. GAAP. While we support the claims incurred recognition model currently employed, we believe the industry and investors would benefit if revenue recognition practices and guidance were refined to allow premium revenue recognition to follow expected claims emergence patterns for monthly pay products, resulting in a similar revenue recognition pattern as single premium products.

- **Reinsurance Accounting** – The criteria to achieve reinsurance accounting is arbitrary and often results in certain reinsurance arrangements being accounted for under a deposit accounting model when in fact insurance risk has been transferred to the reinsurer.
Guidance should be updated to allow such contracts to be accounted for under a reinsurance accounting model.

The items listed above may not be all-inclusive and should be used by the Board in considering the appropriate targeted improvements. More discussion around updating existing guidance and an evaluation of the implications should be part of the deliberation process for making targeted changes.

The benefits of making targeted improvements would be demonstrated by the continuing use of U.S. GAAP as the basis of performance measurements and a lack of significant changes in key metrics that users and companies commonly utilize to evaluate and compare performance, such as loss & expense ratios, premiums, and book value per share. Additionally, targeted improvements would be implemented at a fraction of the cost while still achieving the Board’s objectives of improving and simplifying accounting for insurance contracts.

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We urge the Board to carefully consider our comments expressing concerns with the Proposal and the implication for insurers. The Proposal will result in both significant implementation and ongoing costs, as well as significant volatility within current period net income as a result of changes in projected cash flows that will occur over several periods in the future, with many changes likely over time. By reflecting the impact of these changes in projected, long-duration cash flows within current period net income, the volatility in reported results for many insurers will likely lead to higher costs of capital as a result of insurance companies being perceived as less desirable to investors who may be considering other investment alternatives that will have more stability in reported earnings metrics (such as other financial services entities).

We appreciate the opportunity to comment on the Proposal. If there are any questions regarding the content of this letter or you wish to discuss our comments and recommendations, please contact Matt Farney, Deputy Controller, at (804) 662-2447, Justin Etheridge, Director Accounting Policy, at (804) 922-5084 or me at (804) 281-6321.

Sincerely,

Kelly L. Groh
Senior Vice President, Financial Reporting and Operations; Chief Accounting Officer
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?

We do not object to the proposed definition of an insurance contract and the related increased scope; however, we believe the Board’s objectives could be better achieved through modification of existing guidance.

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?

Existing U.S. GAAP for account value products, which requires separate measurement of the account value and the insurance benefit, more appropriately captures the economic characteristics of these contracts when compared to the Proposal. Should the Board elect to move forward with the Proposal, we would agree with the proposed unbundling requirements, simply based on the additional complexity unbundling of account values would introduce to the proposed measurement model.

The Proposal is unclear on the separation of asset management fees. We suggest the Board clarify that asset management fees should not be separated for contracts such as variable annuities, where fee income is a significant source of revenue and varies with the account value. We do not object to maintaining the existing U.S. GAAP guidance for separation of embedded derivatives but note that the application guidance in Accounting Standards Codification Topic 815 (previously in Derivatives Implementation Group issues) represents an area of difference between U.S. and international accounting which the Board may wish to address.

Questions 3 & 4 Omitted (User Questions)

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?

Losses and the risk that precipitate insured events vary greatly across insurance products and therefore, more than one measurement approach is needed to properly reflect an insurance contract’s economic performance in a given period. With targeted improvements and added disclosures, the foundational measurement principals currently prescribed under U.S. GAAP would better capture and properly report financial transactions occurring in a given period than the Proposal.

Should The Board elect to proceed with the Proposal, the premium allocation approach provides better measurement and more accurately reflects the unpredictable risks, nature and economics of certain insurance products, such as those that insure property and casualty risk. Furthermore, the nature of the risk, not the length of the contract, should dictate the use of the premium allocation approach, which should be optional. For certain insurance contracts, coverages are offered that are at, slightly below and slightly beyond one year. Investors would find accounting for products with similar durations under different models very confusing. Also, it will be costly for insurers to account for these contracts using different methods and systems. Further, modeling of future fulfillment cash flows for certain insurance risks, such as our mortgage insurance business, although possible, are not necessarily predictive of the future due to the nature of the risk insured and their responsiveness to changes in forecasted economic conditions. Measurement of this product under the building blocks approach would not provide dependable decision-useful information to investors.
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?

Permitted use of the premium allocation approach should be based on the risk insured and nature of the insurance product rather than an insurance contract’s duration. Under the Proposal, contracts with indistinguishable risk would be permitted to employ different measurement models – solely based on the duration of the contract. Our mortgage guaranty insurance has historically been accounted for under a claims incurred model due to difficulty in forecasting incidence, frequency and severity of claims. The narrow definition currently proposed for the premium allocation approach will result in certain contracts being measured and reported under an expected loss model, which would provide financial statement users with false sense of precision regarding the businesses future performance.

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?

As indicated in our response to question 6, the permitted use of the premium allocation approach should be principles-based and is currently too narrow under the Proposal. For certain contracts, the frequency, severity and timing of insured events may vary greatly based on circumstances and conditions outside of the insurance company’s control. The proposed language in ASU 834-10-25-18(b), “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” and the related implementation guidance provided in ASU 834-10-55-52 through 55-53 fail to capture certain insurance products that should be included within the scope of the premium allocation approach.

Although the average duration of a mortgage insurance guaranty contract is 5 to 7 years, under most global GAAP and regulatory basis of accounting, claim liabilities have been recognized at the time of delinquency (incurred basis). This recognition pattern is more akin to a short duration accounting model and the premium allocation approach currently being proposed. The frequency, severity and timing of mortgage insurance claims are closely correlated with economic conditions such as unemployment, interest rates and home price appreciation. Although various actuarial techniques are available and used to forecast mortgage defaults, the long tailed nature of mortgage insurance coupled with the unknown economic condition to which the underlying loans will be exposed results in such forecasts often falling short of being predictive. If mortgage insurers had reporting under the proposed building blocks model during the recent financial crises, investors would have been led to believe there was substantial future profitability in these businesses when in fact mortgage insurers had insured the risk that would have eventually nearly bankrupt and collapse many companies within the industry.

The scope for the premium allocation approach should be broadened to allow certain contracts such as mortgage guaranty insurance and longer duration products designed to cover catastrophe type events to be included. We do not believe products that insure non-linear risks where the frequency, severity and timing of insured events may vary greatly based on circumstances or conditions outside of the insurance company’s control can be properly measured and reported under the building blocks approach. Forecasting for these contracts, which will require substantial judgment and assumptions to be made about the future, cannot be accurately predictive and therefore are not useful to investors and financial statement users. Finally, due to the nature of these risks and the dependence of ultimate losses on unknown future events, projections and forecasts of future cash flows would vary widely from company to company and result in financial statements that are not comparable.
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?

We do not agree with the proposed portfolio definition because it will result in a level of granularity that will add significant costs and complexity to the proposed insurance contracts model. The requirement to group contracts that have similar duration and similar patterns of release from risk will result in a significant increase in the number of portfolios compared to current U.S. GAAP as well as the grouping of contracts in a manner inconsistent with how we manage our product lines. For example, we manage term life insurance as a single product line but the “similar duration” requirement would split this product into multiple portfolios for products with 5, 10, 15, 20 and 30 years of guaranteed level premiums. One could also view the similar duration requirement to require disaggregation based on the ages of the policyholders. These changes would greatly increase the complexity as well as the initial and ongoing costs associated with the proposal, with little if any benefit to users.

The objective of a portfolio definition should be consistent with how an entity manages its business. The aggregation rules under current U.S. GAAP, or the definition of a portfolio included in the IASB’s 2013 ED, would achieve this objective. We note that if the Board is concerned about changing patterns of profit emergence by combining contracts, this concern could be addressed within the proposed margin guidance as opposed to changing the definition of a portfolio.

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?

We generally agree with the proposed guidance on contract boundaries but request the Board clarify the treatment where an insurer or reinsurer has the right to increase premiums without limits or up to a maximum amounts specified in the contract. For example, in renewable term reinsurance the pricing is prospective in nature and considers risks relating to future periods. Accordingly, the building blocks approach would be the more appropriate model under the Proposal. However, if the premium cap were high enough to allow for re-pricing to fully reflect the risk of the insurance contracts, then the contract would fall under the premium allocation approach, which would result an accounting mismatch between the reinsurance and the related insurance contracts.

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?

We generally agree with the types of cash flows proposed to be included in the liability measurement but recognize there are differences between the FASB and IASB exposure drafts. We consider these differences to be insignificant and believe they should be eliminated, if the Board elects to move forward with the Proposal.

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?

We generally agree with the proposed guidance requiring the use of current assumptions and believe this language is an improvement over current U.S. GAAP where original assumptions continue to be used for certain products until a premium deficiency test is met. However, we are concerned that updating of assumptions that impact future cash flows would result in significant volatility that could impair the
comparability and usefulness of an entity’s performance measurements. This is especially true for mortgage guarantee insurance that would be under the building blocks approach where the highly subjective projections of future economic conditions could lead to extreme volatility for this product and lack of comparability between competitors that would be difficult for users to understand and interpret. While the updating of assumptions is appropriate, the recognition of those changes in assumptions should be included within the single margin and reflected over time, not immediately.

As stated in our general comments, we continue to believe that improvements could be made to existing U.S. GAAP guidance to reflect the updating of assumptions each period without added costs and complexity that are included in the Proposal.

**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?

We do not object to the building block approach measurement objective of expected value nor the language that clarifies that expected value represents the mean. We agree that probability-weighted estimates are an appropriate method of meeting this objective for forecasts of future cash flows on certain long-duration products. However, the language in 834-10-30 defines fulfillment cash flows in a manner that implies probability-weighted cash flows are required to meet the measurement objective for all liabilities. Probability distributions are not appropriate for certain types of liabilities, for example, our long-term care insurance claim liabilities and mortgage insurance liabilities. It appears the application guidance recognizes that other methods can be used to derive the mean, or expected value. Therefore, we recommend replacing the first sentence of ASC 834-10-30 as follows: The fulfillment cash flows comprise the present value of the unbiased, expected value of future cash outflows less the future cash inflows that will arise as the entity fulfills the insurance contract… .

**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?

We do not agree that changes in projections of future cash flows for insurance contracts should be reflected immediately in net income. Changes in assumptions should be incorporated into the margin due to the long-term nature of our contracts where both positive and negative changes often occur many times over the life of the contract. For example, if our long-term care insurance product exhibits an increase in expected claims, management can file for pricing increases with the regulatory authorities. The increase in expected claims would reduce the economic value of the business while the premium increases would have the opposite effect. However, the ED would require margin amortization based on conditions that existed at the time contracts were issued, as opposed to updated expectations of premiums and benefits. Updating the margin for these assumption changes would provide more useful information to financial statement users than a margin that reflects conditions that no longer exist.

The requirement to reflect changes in the discount rate for certain products outside of net income is necessary given the extreme volatility generated by the proposed discount rate guidance which is unrelated to the performance of insurance contracts.
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?

We disagree with the proposed discount guidance for nonparticipating contracts and urge the board to reconsider requiring a market-based rate. The current discount rate approach for measuring insurance contracts liabilities under U.S. GAAP today recognizes the business models of insurers that issue long-term contracts, which is matching expected cash inflows of a portfolio of assets with the expected cash outflows of insurance contracts. The proposed guidance will provide less useful information to the users of financial statements by failing to reflect this dependence, and by introducing extreme volatility into the financial statements of insurers. We appreciate the decision by the Board to allow changes in the discount rate to flow outside of net income, but the volatility will still have a significant impact on the book value of insurers as a result of not being linked to our expected investment returns. Book value per share is a key metric used today by investors and will no longer be useful as our book value will fluctuate significantly during periods of rapidly changing interest rates.

We recognize there are sound theoretical arguments for various approaches to discounting but urge the board to consider a method that provides useful information to users of financial statements, considers the business model of insurers, and preserves key financial metrics and ratios. From these perspectives, the current approach under U.S. GAAP is significantly better than the proposed discount rate guidance.

Additionally, the proposed discount rate guidance unduly burdens insurers with complexity that is not present elsewhere in U.S. GAAP for similar instruments. For example, certificates of deposits or deposit liabilities of a bank would not be required to apply a current measurement approach based on changes in discount rate. However, a similar product such as a deferred annuity would be forced to apply very complex discount rate guidance in order to measure the insurance liability. The proposed discount rate guidance would place more burden on contracts that are in scope of the Proposal where similar burden and complexity does not exist for other products offered by financial services companies.

We also note the overall model proposed for insurance contracts is extremely complex, and that a significant driver of this complexity is a result of the discount rate guidance, both for participating and nonparticipating contracts.

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?

Discounting of the incurred claims liability should be optional for insurance contracts permitted to use the premium allocation approach. The addition of discounting these liabilities adds unnecessary complexity, additional operational costs, and provides little if any benefit to financial statement users in most instances. In certain instances where discounting of such liabilities is important to investors and analysts, markets would require and insurers would comply with such demands when optionality exists. To require discounting of incurred claims under the premium allocation approach, when in more instances then not discounting is unimportant to the markets, only serves to add operational complexities and additional cost to preparers. If the Board moves forward with a requirement to discount the liability for incurred claims, there should be a more simplified approach that would be permitted in applying the discount rate guidance such as applying a level discount rate or other simplified methods that would not require preparers to perform thorough analysis of the appropriate discount rate using the top-down or bottoms-up approach.
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.

Investment performance is reflective of the business model of insurers and should be presented together with other financial statement items that are related to the performance of portfolios of insurance contracts. The results of the proposed discount guidance are unrelated to the performance of insurance contracts and would be disregarded by users of our financial statements. On this basis, we support the Board’s approach as a necessary step to preserve the relevance of net income. As stated earlier, the current U.S. GAAP approach, which reflects an asset-based rate in net income, provides more useful information to financial statement users than the Board’s proposal.

We also support an option to record changes in the discount rate through other comprehensive income, as opposed to a requirement. We should be permitted to record changes in the discount rate through net income when the corresponding portfolio of assets is measured at fair value through net income.

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?

We do not believe a loss-recognition test specific to the discount rate is appropriate because the measurement basis for the discount rate in the proposal is market-based and unrelated to the performance of insurance contracts. Additionally, we are unsure how an asset-liability mismatch could be quantified or how it would be implemented without adding significant additional complexity to the existing model. We note the proposed discount rate guidance is already complex and challenging to implement without such a test.

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?

While we agree that a specific method for calculating the discount rate should not be prescribed, existing U.S. GAAP for insurance contracts where the discount rate for many contracts is more directly linked to the expected investment performance is a more appropriate basis for determining the discount rate. Using such an approach based on expected investment yields would simplify the discount rate guidance and result in less volatility within the financial statements related to changes in current market rates. The proposed guidance in the exposure draft is understandable but adds significant complexity to the proposed model for insurance contracts and will be very costly to implement, especially if the portfolio definition is not modified and results in a very large increase in the number of portfolios.

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?

We support the current discount rate approach under U.S. GAAP that is based on expected investment yield. If the board were to preserve this guidance, then we would support a current measurement of interest expense. The proposed guidance for nonparticipating insurance contracts, which requires a locked-in discount rate for the income statement, is necessary in order to separate the performance of these insurance contracts.
contracts from unrelated market-based changes in the discount rate. As a result of using the expected investment yield as the discount rate, the interest expense would be more comparable to investment income that is recognized each period and should be relatively consistent if an entity is achieving its expected investment yield at inception of the portfolio.

**Question 20:** Do you agree that upon any change in expectations of the crediting rates used to measure the insurance contract liability for insurance contracts with discretionary participation features, the interest accretion rates should be reset in a manner that recognizes any changes in estimated interest crediting and related expected cash flows on a level-yield basis over the remaining life of the contracts? If not, what do you recommend?

The proposed discount rate guidance for participating contracts would be extremely complex and burdensome for preparers to implement and would fail to provide any incremental benefit to financial statement users. A more appropriate approach would be to retain existing guidance for account value products and focus on any improvements that are deemed necessary by the Board.

If the Board moves forward with the proposal, we agree that changes in expectations of future crediting rates should be reflected prospectively in the income statement, but recommend the Board avoid prescribing a specific method for updating the interest accretion rate. While the method proposed in the model may be appropriate for some products, it is operationally very difficult for others. Specifically, complex modeling techniques employed by insurers that project cash flows based on dynamic interest assumptions and lapses would likely project crediting rates on a non-level basis. In some cases, a projection of expected future crediting rates provides a better accounting match than using a level rate.

The Board prescribed a general principle for setting the initial discount rate for participating contracts and should use a general principle for updating the discount rate for participating contracts. We do not object to leaving the level yield concept in the application guidance as an example.

**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?

Insurers should be prohibited from recognizing a gain upon initial recognition of an insurance contract. The foundational measurement models within current U.S. GAAP, which are less complex and well understood by investors, provide a better measurement and also prevent a gain upon initial recognition. While we recognize the Proposal would similarly result in deferring a gain upon initial recognition, the inclusion of the margin in the financial statements upon initial recognition may provide a false sense of reliability in the entity’s expected future profitability that could and will likely change significantly over time. For example, our mortgage insurance contracts would have initially shown substantial margin/deferred gains in 2006/2007 under the Proposal where our profit margin on these contracts would change substantially in future years. By providing a measurement of the insurance contracts margin in the financial statements, users may imply a level of precision or reliability that may not be appropriate and could be viewed as provided forward looking information on an entity’s future performance that would not be protected by the Safe Harbor rules that accompany MD&A disclosures for SEC registrants.

**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.
We support an implicit margin approach consistent with today’s U.S. GAAP measurement models. If the Board moves forward with the Proposal, we support using a one-margin approach but believe the one-margin approach proposed by the FASB should be modified to allow for unlocking of the margin. See response to Question 23 for more discussion related to unlocking of the margin.

An explicit risk adjustment margin should not be included in the proposed measurement approach. Risk margins are very subjective and result in inconsistent measurements among similar financial statement prepares. Furthermore, explicit risk margins are a concept used in fair value measurements and are inconsistent with the concepts of fulfillment cash flows.

**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?

Notwithstanding our disagreement with the inclusion of an explicit risk adjustment in the measurement model as noted in our response to Question 22, changes in estimates of future cash flows should adjust the margin. Failure to recalibrate the margin for changes in estimates of future fulfillment cash flows would be inconsistent with the re-measurement principle used for the other building blocks of the Proposal.

The ED is built on the premise that measurement of future expected cash flows is paramount to financial reporting for insurance contracts and concludes that changes in that measurement should be the primary driver in reporting current period results. While we appreciate the desire to have insight on embedded value, we disagree that such a measure should be the basis for financial reporting. It is our belief investors and users of financial statements have little appetite and desire for a new measurement model where earnings are based on forecasts of the future. Current U.S. GAAP measures long-duration contracts and records a liability for future policy benefits based on the present value of future claims and expenses less expected net premiums. For traditional contracts, this liability is recorded based on contractual consideration (premiums) due from policyholders. One of the primary issues investors have with this model—where assumptions and the related margin are locked-in at issuance and can only be changed in the event of premium deficiency—would continue to exist under the proposed model because the margin (profit) would remain locked-in and only changed if a contract becomes onerous (deficient). Accordingly, we support unlocking of the margin to avoid unnecessary complexities in understanding an entity’s performance and believe unlocking of the margin would provide more decision useful information to investors under the Proposal.

**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?

An expected loss at initial recognition (or at any other time during the life) of a portfolio of insurance contracts should be recognized immediately in net income. Similar requirement currently exists within U.S. GAAP within ASC 944.

While we agree that losses should be recognized in net income at inception for a portfolio of contracts, there could be instances where losses may exist solely due to the discount rate guidance not considering an entity’s expected investment returns. Both participating and non-participating long-duration insurance contracts are priced considering investment income, and we believe it is inappropriate to record a loss at inception on contracts that are expected to be profitable.
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?

If the Board moves forward with the Proposal, we recommend removing the guidance referencing the release from risk related to the reduction in variability of cash flows and using methods similar to the IASB’s proposed guidance on margin recognition. The FASB’s margin recognition criteria (when released from risk evidenced by the reduction in variability of cash flows) prescribed in this proposal seems overly punitive and overly prescriptive. As noted above under the FASB’s proposal, insurers of long-duration contracts would be required to push profit recognition to the tail end of most contracts, while insurers reporting under IFRS would be permitted to recognize margins “over the coverage period in the systematic way that best reflects the remaining transfer of services that are provided under the contract.” The IASB margin recognition guidance would permit insurers to recognize margin over the life of the contract for the administrative and investment services performed – which for long-duration contracts are critical functions that are diligently performed over the life of the contract.

We support existing recognition models in current U.S. GAAP, which effectively results in recognizing the margin as premiums are collected. Although, as mentioned earlier in our letter, we recognize targeted improvements could be made in order to unlock assumptions (as conditions warrant). The proposed change in revenue recognition from existing guidance is not warranted nor desired by users. While the Proposed guidance may result in a theoretically sound approach and be consistent with more recent proposals on revenue recognition, there are other examples in existing accounting guidance where earnings are based on when contractual amounts are due (interest income recognition of loans) where the information provided is considered decision-useful and is not under consideration for change.

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

Under the current FASB proposal interest should be accredited on the margin. Absent accretion, the locked in margin, which is calculated at the inception of the contract based on the present value of future cash flows, would produce understated profitability within earnings over the life of the contract.

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?

We do not support recognizing the remaining margin in net income when expected cash outflows exceed expected cash inflows. As stated in our response to question 23, we support unlocking of the margin for all changes in expectations of future cash flows (both positive and negative), which would render a loss recognition test unnecessary. On a conceptual basis, we do not believe it makes sense to recognize a gain (by accelerating margin recognition) as the result of a loss recognition test. Additionally, the result would create an accounting mismatch, where the adverse changes in expected future cash flows would be recorded over time through net income and the margin release would be recorded all at once in a single period. This would also create significant inconsistencies between companies’ reported results, as inherit differences in views on the frequency and extent of cash flow assumptions changes will drive very different recognition of the remaining margin. For example, if preparers see the same short-term trends during a year, one company may decide to change assumptions immediately reflecting smaller adjustments to net income, while another company may wait to reflect new, short-term trends until there is more, or adequate, evidence supporting that assumption change. Under the proposal, this may result in the company that waited releasing the remaining margin in net income not having expected cash outflows exceeding expected cash inflows in any
period. Finally, the test would necessitate maintaining records of historical cash flows for all contracts in order to determine when the loss trigger is met. The costs of maintaining these records would be significant compared to what we perceive as very little benefit from the guidance.

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?

We support a definition for deferred acquisition costs including only successful efforts, consistent with existing U.S. GAAP given the relatively recent changes that were made. Given the time and costs, including system changes, as well as the educational efforts for users that were recently employed on adopting the recent changes in deferred acquisition costs, another change in the definition for deferred acquisition costs is not warranted for U.S. stakeholders.

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?

We do not agree that the measurement of the margin for contracts using the building block approach should be directly reduced for direct acquisition costs incurred. Acquisition costs should be treated like any other cash outflow in determining the margin. The separate presentation of acquisition costs as a reduction to the margin adds unnecessary complexity to the presentation and is inconsistent with the building block approach, as acquisition costs meet the definition of fulfillment cash flows. This is an area where the FASB and IASB could easily converge their separate proposals.

We support reflecting acquisition costs in the liability for remaining coverage under the premium allocation approach.

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?

As stated in our response to Question 29, acquisition costs should be included in the measurement of expected future cash outflows. However, if the Board moves forward with the proposal to reduce the margin by acquisition costs incurred, then we would agree that acquisition costs should be recognized in the same pattern as the margin or liability for remaining coverage.

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?

Traditional financial statement metrics for insurers such as premiums, benefits and related expenses, acquisition costs and changes in reserves are the primary measures used by analysts and investors in insurance companies to evaluate the performance of insurers and by management to assess actual performance of different components. On this basis, they should be presented on the face of the financial statements.
The current U.S. income statement presentation provides useful information to financial statement users about the performance of our insurance business. The proposed income statement approach is not an improvement to existing guidance, and on the contrary, will degrade the relevance of information presented in the income statement. Financial statement presentation should not be industry specific. That is, a large conglomerate company should be able to present insurance results along with different businesses.

The concept of insurance revenue being recognized as an entity is released from risk is a hypothetical calculation that when combined with the guidance for separating the estimated returnable amount, results in a number that will be extremely difficult for preparers to explain, and even more difficult for investors and analysts to understand. Additionally, the proposed revenue approach will be very costly to implement, as we will be required to make costly modifications to our administrative systems to accommodate the significantly increased data requirements resulting from this measurement.

We recommend the Board require premiums to be presented as a component of underwriting performance, and that the board does not otherwise prescribe a specific income statement presentation, beyond listing what items are required on the face of the financial statements.

**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.**

We do not object to removing premiums from the income statement for products with explicit account values but believe this goal could be achieved by retaining existing U.S. GAAP that would exclude the amount that accrues to the policyholder from the determination of premiums. The current approach under U.S. GAAP results in the cost of insurance and other charges being reflected as revenue on an accrual basis, a concept consistent with how we price and manage these products, that also has the benefit of being easy to understand.

We disagree with the proposed approach for excluding estimated returnable amounts from revenue presented in the income statement because it is extremely complex and costly to implement, and combined with the guidance for unwinding revenue in the income statement, will result in revenue measure that does not provide useful information to investors and analysts. The proposed overall insurance contracts model will be very difficult to understand; since the revenue measure will not have any impact on net income, it should not add additional complexity to the model, but rather provide users with financial information that is relevant and easy to understand.

We also disagree with the requirements to exclude estimated returnable amounts from revenue for non-account value products such as whole life insurance, immediate annuities with term certain and products with return of premium riders because doing so would not provide more useful information to financial statement users than the current U.S. GAAP premium approach.

We estimate significant costs associated with reprogramming our administrative systems to separate revenue on the wide range of product features this proposal will apply to. The costs of determining the initial estimated returnable amount, as well as updating it each period far outweigh any benefit provided to financial statement users.

**Question 33: For contracts measured using the premium allocation approach, do you agree that if the contract has a financing component that is significant to the contract, an entity should adjust the liability for remaining coverage to reflect the time value of money and recognize the accretion of interest with insurance revenue? Do you agree with the practical expedient that an entity should not**
be required to reflect the time value of money in measuring the liability for remaining coverage (that is, if the entity expects, at contract inception, that the time period between when the policyholder pays all or substantially all of the premium and when the entity provides the corresponding part of the coverage is one year or less)? If not, what do you recommend and why?

The liability for remaining coverage for contracts measured under the premium allocation approach should be discounted to reflect the time value of money when the insurance contract contains a significant financing element and the impact of discounting is material. While we appreciate the Board including a practical expedient to avoid discounting for contracts where premiums are paid within one year, we recommend a more conceptual approach of determining when such elements are material that is not strictly based on a time period of when premiums are expected to be paid. Such an approach could be based on how an entity evaluates the product performance to determine whether discounting should be required. Even when discounting is required for contracts under the premium allocation approach, a practical expedient should be included that would enable the use of a level discount rate or other simplified method.

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.

As discussed in our response to question 31, premium recognition as provided for under current U.S. GAAP provides a valuable measurement metric heavily relied upon by the insurance industry and analysts. To replace this approach with a hypothetical calculation seems arbitrary, potentially inconsistent amongst insurers, and leaves the investors and analysts without a relevant income statement metric to analyze customer consideration. We do not agree with the theory behind the determination of insurance contracts revenue.

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?

We agree with the guidance for participation features where there is a contractual linkage between the performance of assets and the related insurance contract liabilities, as it results in an appropriate measurement for separate account products. However, we are concerned with the requirement to present investment income and interest credited to policyholders on a net basis in the income statement. See our response to Question 40. We also believe the current U.S. GAAP approach for measurement of account values should be retained for all products, including those where there is discretion in the amount credited to policyholders. An account value liability plus a liability for additional benefits provides more decision-useful information than a single liability based on expected cash flows.

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?

We agree with the prohibition of any gain or loss at inception of a reinsurance contract but believe an exception should be made for reinsurance of new business where there is a loss at inception on the direct contract that will be recognized in net income. Permitting a gain on reinsurance up to the amount of the loss will eliminate an accounting mismatch where the impacts of two equal and offsetting contracts are reported in different time periods.

**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?

We agree with the measurement guidance for reinsurance contracts because it results in a measurement consistent with measurement of the reinsured insurance contracts.

**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?

We disagree with the guidance that would require a loss to be recorded in a business combination and believe any loss should be treated as an adjustment to goodwill. We agree that entities should record a margin and not recognize an immediate gain. We do not see any compelling reason why insurance contracts should be treated inconsistent with any other assets or liabilities under the business combination guidance.

**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?

We disagree with the proposed guidance because it is too complex and would be very difficult to implement. The guidance would force us to examine each substantially modified contract individually and determine a theoretical price. We would then have to track each contract separately going forward. We support either maintaining current U.S. GAAP guidance for contract modifications or the proposal outlined by the American Council of Life Insurers in their comment letter, which would conform existing U.S. GAAP for contract modifications to the proposed measurement model while removing some of the complexities.

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

We do not agree with the proposed presentation requirements because they are overly prescriptive and dramatically change many of the key performance metrics that currently exist and are used by analysts and
investors to evaluate our performance. The existing U.S. GAAP guidance related to presentation should be retained as it reflects earnings in a manner consistent with the economics of our businesses.

If the Board moves forward with the proposal, we recommend considering an approach that would align presentation with the way premiums and other common measures are presented today. Such a presentation approach could be applied while still maintaining the net income impact that would occur under the proposal. In addition to reducing costs and complexity, an approach that continues to leverage information similar to existing U.S. GAAP today would avoid entities having to prepare separate non-GAAP measures to explain key performance measures that would otherwise be obscured within the proposed presentation.

We are also concerned with proposed presentation for contractually dependent participating contracts (such as separate accounts) and believe the proposal should retain the net presentation that is utilized today to avoid investor confusion or inflated income statement lines. Insurers act as an agent in these separate account transactions when they pass the investment income to the policyholders and a gross financial statement presentation would fail to reflect this relationship. The impact of this gross up would also result in sizable volatility within income statement line items, which will complicate analysis of those line items and cloud the presentation of actual performance.

**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?

We do not agree with the proposed disclosure requirements and believe they would be overwhelming and difficult for users to understand while significantly impairing our ability to produce financial statements in the timeframe required by the SEC. While we recognize that improvements could be made to existing disclosure guidance, the Board should evaluate the usefulness and purpose of each disclosure in terms of information that is desired by financial statement users and balance those desires with the costs that would be incurred by preparers.

Additionally, we are concerned with the forward looking nature related to certain disclosure requirements to show the amount of expected fulfillment cash flows segregated into time intervals as well as the sensitivity analysis on key assumptions. We recognize that this disclosure is similar to what was proposed in the Liquidity and Interest Rate Disclosure project, which is currently inactive while the Board is considering the objective of the project. Similar to our concerns with this disclosure proposal in 2012, we are concerned with including forward looking information in our financial statement disclosures, which are not afforded the same protections under the SEC’s safe harbor rules that apply to disclosures within MD&A of public company filings. Introducing similar types of disclosures for insurance contracts to those that were included in the 2012 disclosure proposal would be inappropriate and should be deferred for consideration as a part of the reconsideration of the objective for the existing inactive disclosure project. By including such disclosures within the insurance contracts proposal, insurance entities would be faced with undue costs and burden while other financial institutions would not be required to disclose similar types of projected cash flows that would be forward looking in nature.

**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?
We have certain products where existing systems are not capable of producing the information required under the proposal. Certain other product lines may have some of the capabilities that are necessary but processes would need to be further enhanced to produce the necessary iterations of information in the time frame required for the quarterly and annual reporting processes and consistent with Section 404 of the Sarbanes-Oxley Act. Many of the aspects that make the proposed model complex to apply are compounded in having to address those complexities and assumptions when determining the impact upon transition. The complexities that impact implementation the most relate to the locked-in margin (as opposed to having an unlocked margin), definition of a portfolio (likely will require significant disaggregation compared to existing guidance), the discount rate guidance, determining the estimated returnable amounts and the onerous contracts test. In the event that changes are made to these items above that would better align with existing guidance, the implementation costs and time needed to implement the proposal would be reduced. Should the Board elect to move forward with the proposed guidance, a minimum of 48 months would be needed to implement and retrospectively adopt the standard.

Question 43: Do you think the effective date should be the same for both public and nonpublic entities? Do you think the effective date should be the same for regulated insurance entities and other entities that issue insurance contracts within the scope of this proposed guidance? Why or why not?

The time necessary to implement the proposed guidance should apply equally for all entities and should be effective at the same time.

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?

We appreciate the Board’s inclusion of several practical expedients to allow for easier application upon transition and believe such practical expedients should be retained if the Board proceeds with the Proposal. With respect to the ability to utilize the existing portfolio definition prior to the effective date in determining the measurement of the liability, we support this practical accommodation in being able to make transition easier. However, it is not clear how this type of aggregation should be applied with respect to determining the locked-in margin and locked-in discount rate for portfolios that span over several years. On the surface, the ability to keep the existing definition of the portfolio would alleviate the burden of having to go back through and re-create a more disaggregated view of the portfolios and assumptions; but it is not clear how one should determine the margin and locked in discount rate upon transition for this broad portfolio definition without effectively performing the more disaggregated and extremely time consuming evaluation of the assumptions that would have been used at issuance. Similar to our comments in Question 42, such question could be greatly reduced if the margin was continually unlocked and if the discount rate were tied to expected portfolio yield.

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?

The transition provisions for business combinations that occurred before the transition date are not operable for business combinations completed many years ago. Unlike products issued more recently where original pricing information or documentation would exist, the assumptions used in business combinations to determine the margin and fulfillment cash flows likely will not be available for older transactions. A practical expedient could be applied in those instances where information is not available related to prior business combinations to allow an entity to measure the contracts as of the earliest period presented to establish the measurement of these contracts. In the event the Proposal is modified to reflect an unlocked
margin, this resulting presentation will be relatively consistent with the measurement of contracts that were not acquired and would be less costly for preparers to determine the impact upon transition.

**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?

The approach to transition will not provide relevant and useful information to users as a result of the concerns we have with certain key aspects of the ED. The existence of a locked-in margin and discount rate based on current rates, as opposed to expected portfolio yields, effectively results in a measurement within the balance sheet that would not result in the margin component representing the future profitability that an entity expects. While these issues are more inherent in the proposed model, the lack of providing decision useful information in the proposed measurement objective would also carry over the balances that would exist upon transition.

**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 terms of incremental costs upon adopting the guidance, we anticipate that the dedicated resources, significant system modifications and enhancements to processes and related controls over financial reporting will result in a cost that would be more than $100 million over a four year time period from finalization of the proposed guidance to the effective date. These costs do not include any external costs that may result from higher audit fees and could increase exponentially if the implementation timeframe is condensed, as many companies would be competing for the same resources thus driving the costs up.

Our estimate of costs were developed based on discussions with product line managers and understanding existing capabilities as well as making assumptions about the resources that would be needed across the organization. It is possible that the costs could be significantly higher than $100 million. These excessive costs far exceed any benefits that would result from adopting the Proposal when targeted improvements to existing U.S. GAAP could be made and minimize the additional costs that would be incurred by preparers.

With respect to ongoing costs, we have estimated these amounts could be in excess of $25 million annually using similar methods to the ones described for the costs for adopting the guidance.

The costs associated with the significant resources and system/process enhancements noted above are primarily the result of the proposed guidance on portfolio aggregation, locked-in margin, discount rate methodology (including the OCI guidance), and income statement presentation. The proposed guidance on portfolio aggregation coupled with locked-in margin and discount rate are expected to result in much more disaggregated portfolios than what our systems are designed to measure and retain today. By modifying the portfolio definition to be more closely aligned with the existing guidance for aggregating groups of contracts for premium deficiency testing today, there would be less system modifications or process enhancements that would be needed to apply the proposed guidance.

Similarly, the locked-in margin could be unlocked each period and would reduce the burden of trying to capture that amount at inception of the contract and develop the appropriate amortization pattern. While there would still be complexity and costs associated with an unlocked margin, utilizing an approach with an unlocked margin would be preferable and would avoid having to retain historical margin amounts that are locked in at inception and amortized over time.
For the discount rate guidance, the complexity involved in determining the discount rate far exceeds the complexity that is involved in the existing guidance where the expected portfolio yield is utilized as the basis for the discount rate. The Board could modify the discount rate guidance to reflect the expected portfolio yield and avoid significant costs that would be required to apply the discount rate guidance and the changes that would occur each reporting period as a result of the changes in discount rate from market rate movements.

The income statement presentation could be improved by removing the requirement to separate the estimated returnable amounts and derived calculation of insurance contracts revenue. The complexity and processes that would need to be implemented to comply with these requirements are significant. The Board should retain existing guidance for income statement presentation with respect to excluding amounts that accrue to the policyholder (for account value products) and income statement line items to ensure historical performance measures would be preserved.

While the Proposal could accommodate the suggest improvements we have recommended for these items herein thereby significantly reducing the costs associated with the Proposal, the remaining costs would still far outweigh any benefit from the new guidance.