**FASB Emerging Issues Task Force**

**Issue No.** 09-G

**Title:** Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts

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**Background**

1. Insurance entities often incur costs that meet the definition of acquisition costs included in Topic 944, Financial Services-Insurance. Acquisition costs are defined in the Master Glossary of the FASB Accounting Standards Codification™ as:

> Costs incurred in the acquisition of new and renewal insurance contracts. Acquisition costs include those costs that vary with and are primarily related to the acquisition of insurance contracts.

2. The implementation guidance in paragraph 944-30-55-1 provides the following three examples of acquisition costs that "vary with and are primarily related to" insurance contracts issued or renewed during the period in which those costs are incurred:

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* **The alternative views presented in this Issue Summary Supplement and Working Group Report are for purposes of discussion by the EITF. No individual views are to be presumed to be acceptable or unacceptable applications of Generally Accepted Accounting Principles until the Task Force makes such a determination, exposes it for public comment, and it is ratified by the Board.**

a. Agent and broker commissions
b. Salaries of certain employees involved in the underwriting and policy issue functions
c. Medical and inspection fees.

3. Costs incurred by insurance entities that meet the definition of acquisition costs in Topic 944 are recognized as assets and are commonly referred to as deferred acquisition costs, or DAC. DAC assets are amortized over time using methods of amortization dependent upon the nature of the underlying insurance product (that is, in proportion to premium revenue recognized, based on a contract's estimated gross profit/margin, and so forth) as prescribed in Subtopic 944-30-35, Financial Services-Insurance-Subsequent Measurement. Other costs, such as those relating to investments, general administration, and policy maintenance, that do not vary with and are not primarily related to the acquisition of new and renewal insurance contracts should be charged to expense as incurred.

4. The accounting policies for DAC of insurance entities have varied in practice. That diversity can be partially attributed to interpretations of the phrase "vary with and are primarily related to" within the definition of acquisition costs. In addition, there are other questions related to whether certain types of indirect costs, such as advertising, would be considered "primarily related to" the acquisition of new and renewal insurance contracts. Thus, while the guidance in Subtopic 944-30, Financial Services-Insurance–Acquisition Costs, provides some examples of acquisition costs, the definition of what constitutes an acquisition cost can be interpreted in different ways.

5. As a result of the diversity in practice relating to the interpretation of what costs qualify as acquisition costs within the insurance industry, certain constituents initially raised the question of whether advertising costs meet the definition of acquisition costs. However, given that the conceptual issue of how to interpret the phrase "vary with and are primarily related to" is broader and applies to more than advertising costs, this Issue is not limited to advertising costs.

**Prior EITF Discussion**

6. At the November 19, 2009 EITF meeting, the Task Force reached a consensus-for-exposure on this Issue that specified the types of costs incurred in the acquisition of new and renewal insurance contracts that would be capitalizable by insurance entities using a model similar to the accounting for loan origination costs in Subtopic 310-20, Receivables-Nonrefundable Fees and Other Costs. Accordingly, the following guidance was included in the consensus-for-exposure, which identified capitalizable acquisition costs as:

> 1. Incremental direct costs of contract acquisition. Incremental direct costs are those costs that result directly from the acquisition of the contract and would not have been incurred by the insurance entity if the contract had not been acquired.
>
> 2. Certain costs directly related to the following acquisition activities performed by the insurer for the contract:
>     i. Underwriting
>     ii. Policy issuance and processing
>     iii. Medical and inspection
>     iv. Contract selling.
>
> The costs directly related to those activities include only the portion of an employee's total compensation and payroll-related fringe benefits directly related to time spent performing those activities for actual acquired contracts and other costs related to those activities that would not have been incurred if the contract had not been acquired.
>
> All other acquisition-related costs—including costs incurred by the insurer for soliciting potential customers, market research, training, administration, unsuccessful acquisition or renewal efforts, and product development—would be charged to expense as incurred. Administrative costs, rent, depreciation, occupancy, equipment, and all other general overhead costs would be considered indirect costs and would be charged to expense as incurred.

7. The consensus-for-exposure also required that advertising costs be accounted for under Topic 720, Other Expenses, or Subtopic 340-20, Other Assets and Deferred Costs—Capitalized Advertising Costs, as applicable, and not be included as deferred acquisition costs.

8. At the March 18, 2010 EITF meeting, the Task Force considered the comment letters received resulting from its consensus-for-exposure. The Task Force affirmed its consensus-for-

exposure that acquisition costs should include only those costs that are directly related to the acquisition of new or renewal insurance contracts by applying a model similar to the accounting for loan origination costs. The Task Force also affirmed its consensus-for-exposure that costs related to unsuccessful contract efforts should be expensed and that advertising costs should only be capitalized if the criteria for capitalizing such costs pursuant to the direct-response advertising guidance in Subtopic 340-20 are met.

9. Task Force members also discussed a comment received from a preparer who believes that the proposed guidance would require some property and casualty insurers to defer additional costs under the revised model over what are currently being deferred in practice under the current model for DAC. The Task Force tentatively concluded that entities should not be required to capitalize additional costs as a result of applying the proposed guidance. Additionally, the Task Force requested that the staff perform research on whether its decision that advertising costs should only be capitalized if the criteria in Subtopic 340-20 are met could impact the premium deficiency analysis performed by insurance entities as required in Subtopic 944-60, Financial Services-Insurance-Premium Deficiency and Loss Recognition, or the analysis of the realizability of the amounts of direct-response advertising that is required under Subtopic 340-20. Lastly, the Task Force requested that the staff perform research on the efforts required and methodologies that could be used to implement the proposed model to assist in its discussion of the effective date and transition methods of the proposed guidance.

10. A Working Group was formed to assist the staff in advising the Task Force on the effective date and transition questions. The Working Group met on May 13, 2010, and its members included preparers and auditors of life insurance and property and casualty insurance entities, a life insurance industry association representative, and an observer from the Securities and Exchange Commission. Several Task Force members also observed and participated in the meeting. The Working Group's report from this meeting is attached to this memo as Appendix 09G-A. The staff also visited with representatives from a life insurance entity. The feedback received by the staff in that meeting was consistent with the discussions of the Working Group that are summarized in the attached appendix. Additionally, the staff performed outreach to users of insurance company financial statements to accumulate additional information to assist

the Task Force with their upcoming discussions on the effective date and transition methods of the proposed Update.

11. At the July 29, 2010 EITF meeting, the staff will present various items to the Task Force for it to consider in proceeding with this Issue. The Task Force will be asked to conclude on how an insurance entity should incorporate the future cash flows attributable to advertising costs for an insurer's premium deficiency analysis and its assessment of the realizability of capitalized direct-response advertising costs. Additionally, the Task Force will be asked to finalize its views on the transition methods and disclosures as well as the effective date of the proposed Update. Lastly, the Task Force will be asked to approve the drafting changes suggested by the staff to the Amendments to the Codification that were originally included in the Task Force's consensus-for-exposure, included as Appendix 09G-B to this memo.

**Accounting Issues and Alternatives**

**Issue 1: How an insurance entity should incorporate future cash flows attributable to advertising costs in its premium deficiency analysis and assessment of the realizability of direct-response advertising.**

12. The accounting guidance for advertising costs included in Subtopic 720-35, Other Expenses-Advertising Costs, does not address the accounting for direct-response advertising, but, rather, refers to Subtopic 340-20 for direct-response advertising whose primary purpose is to elicit sales to customers who can be shown to have responded specifically to the advertising and results in probable future benefits. Paragraph 340-20-25-6 discusses the conditions that must exist in order to conclude that the advertising's purpose is to elicit sales to customers who could be shown to have responded specifically to the advertising and states that there must be a means of documenting that response, including a record that can identify the name of the customer and the advertising that elicited the direct response. Examples of such documentation include the following:

a. Files indicating the customers' names and the related direct-response advertisement

b. A coded order form, coupon, or response card, included with an advertisement, indicating the customers' names
c. A log of customers who have made phone calls to a number appearing in an advertisement, linking those calls to the advertisement.

13. Paragraph 340-20-25-9 discusses the conditions that must exist in order to conclude that direct-response advertising results in probable future benefits. Demonstrating that direct-response advertising will result in future benefits requires persuasive evidence that its effects will be similar to the effects of responses to past direct-response advertising activities of the entity that resulted in future benefits. Such evidence includes verifiable historical patterns of results for the entity. That paragraph also provides the following attributes to consider in determining whether the responses will be similar:

a. The demographics of the audience
b. The method of advertising
c. The product
d. The economic conditions.

14. Under the aforementioned guidance, if the criteria for direct-response advertising are met, the costs are capitalized and amortized. The costs are amortized on a cost-pool-by-cost-pool basis over the period during which the future benefits are expected to be received using the ratio that current period revenues for the direct-response advertising cost pool bear to the total of current and estimated future period revenues for that direct-response advertising cost pool. Additionally, paragraph 340-20-35-3 states the following:

a. The amounts in that calculation shall not be discounted to net present value.
b. The estimated amounts of future revenues for that cost pool may increase or decrease over time, and the ratio shall be recalculated at each reporting date.
c. Changes in estimated future revenues for a direct-response advertising cost pool shall be reflected in the amortization calculation for current and future periods.

15. For advertising costs that are capitalized by entities under the guidance in Subtopic 340-20, a realizability test of the direct-response advertising is also required. Paragraphs 340-20-35-4 and 35-5 describe the realizability analysis of direct-response advertising costs below:

> The realizability of the amounts of direct-response advertising reported as assets shall be evaluated at each balance-sheet date by comparing the carrying amounts of such assets on a cost-pool-by-cost-pool basis to the probable remaining future net revenues expected to result directly from such advertising. (For this evaluation, future net revenues are gross revenues less the probable future costs of all goods and activities necessary to earn those revenues, except amortization of direct-response advertising. Examples of such future costs are the costs of goods sold, sales commissions, and payroll and payroll-related costs associated with the future revenues.) If the carrying amounts of such advertising exceed the remaining future net revenues that probably will be realized from such advertising, the excess shall be reported as advertising expense of the current period. The reduced carrying amounts shall not be adjusted upward if estimates of future net revenues are subsequently increased.
>
> There is no arbitrary limit of the period over which the direct-response advertising shall be amortized. However, the reliability of accounting estimates decreases as the length of the period for which such estimates are made increases. Therefore, the period over which the benefits of direct-response advertising are amortized often is no longer than the greater of one year or one operating cycle. However, under certain circumstances, an entity may be able to demonstrate that the duration of the probable future benefits is greater than the longer of one year or one operating cycle. For example, while the response to advertising usually occurs shortly after the advertising takes place, in mail-order catalogue advertising, it can take place over a longer period.

16. The staff believes that some insurance entities are capitalizing advertising costs as DAC pursuant to Subtopic 944-30. Under that Subtopic, capitalized acquisition costs must have been incurred in the acquisition of new and renewal insurance contracts and demonstrated to vary with and be primarily related to the acquisition of new and renewal insurance contracts. As capitalized acquisition costs, the costs are deferred and charged to expense in the following manners dependent upon the nature of the underlying insurance product:

a. Proportional to revenues (short-duration)
b. Using methods that include the same assumptions used in estimating the liability for future policy benefits (long-duration).

17. There are two premium deficiency analyses required by Subtopic 944-60 depending on whether the underlying contract with the policy holder is short-duration or long-duration in nature. If the contract is short-duration, a premium deficiency is recognized if the sum of expected claim costs and claim adjustment expenses, expected dividends to policyholders, unamortized acquisition costs, and maintenance costs exceeds related unearned premiums. For long-duration contracts, a premium deficiency is recognized if existing contract liabilities taken together with the present value of gross premiums are not sufficient to cover the present value of future benefits to be paid to policyholders and maintenance costs relating to a block of long-duration contracts and to recover unamortized acquisition costs. The following tables illustrate how premium deficiencies are calculated for both short-duration and long-duration contracts:

*Short-Duration Contracts*

| | | |
|---|---|---|
| Expected claim costs | | $XXX |
| Claim adjustment expenses | | XXX |
| Expected dividends to policyholders | | XXX |
| Unamortized acquisition costs | | XXX |
| Maintenance costs | | XXX |
| | A | $XXX |
| Unearned premiums | B | $XXX |

If A is > B, a premium deficiency exists.
If A is < B, no premium deficiency exists.

*Long-Duration Contracts*

| | |
|---|---|
| Present value of future payments for benefits and related settlement and maintenance costs, determined using revised assumptions based on actual and anticipated experience | $XXX |
| Less the present value of future gross premiums, determined using revised assumptions based on actual and anticipated experience | $XXX |
| Liability for future policy benefits using revised assumptions | $XXX |
| Less the liability for future policy benefits as the valuation date, reduced by unamortized acquisition costs | $XXX |
| Premium Deficiency or (Surplus) | $XXX |

18. As a result of the Task Force's consensus that advertising costs should only be capitalized if the criteria for capitalizing such costs pursuant to the direct-response advertising guidance in Subtopic 340-20 are met, it is not clear how insurance entities should incorporate the future cash flows attributable to those advertising costs in their premium deficiency analyses as well as in their assessments of the realizability of the amounts of direct-response advertising that are required under Subtopic 340-20.

19. The staff considered whether a possible solution to the issue of how an insurance entity should incorporate the future cash flows attributable to those advertising costs in its premium deficiency analysis as well as its assessment of the realizability of the amounts of direct-response advertising would be to exclude any direct-response advertising from DAC and require that insurance entities follow the advertising guidance in Topic 720 or Subtopic 340-20, as applicable. However, the staff believes that this approach would be problematic because the direct-response advertising may not be the only capitalized cost associated with acquiring or renewing a contract. For example, as a result of contract acquisition and renewal efforts, an insurance entity may have capitalized direct-response advertising costs as well as other acquisition costs, such as commissions, as part of DAC. Therefore, requiring the direct-response advertising costs to be separated from DAC when entities perform their direct-response recoverability and premium deficiency tests, would require a bifurcation of the cash flows to be used to support the recoverability of both the direct-response and remaining DAC assets. Given the complexities associated with such a methodology, the staff prepared two alternative methodologies that would provide insurance entities with guidance on how to perform both analyses.

*Staff Analysis*

*View A: Utilize the direct-response advertising guidance in Subtopic 340-20 for capitalization purposes, and then treat the capitalized costs as deferred acquisition costs pursuant to Subtopic 944-30 for classification, subsequent measurement, and premium deficiency purposes.*

20. Proponents of View A believe that this methodology provides preparers with a reasonable approach for supporting the recoverability of the direct-response advertising in a less complex manner than the approach proposed in View B. Additionally, proponents of View A believe that this methodology would result in a minimal change for insurance entities that are currently capitalizing advertising costs as DAC pursuant to Subtopic 944-30, provided those acquisition costs will meet the direct-response capitalization criteria in Subtopic 340-20 as prescribed by the proposed Update. However, opponents of View A believe that if an entity is required to use the capitalization criterion for direct-response advertising to determine whether an advertising cost can be capitalized, then the recoverability test applied to direct-response advertising should also be used to assess the recoverability of that asset.

21. Additionally, opponents of View A believe that property and casualty insurance entities will be disadvantaged by the methodology in View A. For example, if a property and casualty insurer currently capitalizes direct-response advertising under Subtopic 340-20, that entity is required to utilize a realizability model that includes probable remaining future net revenues expected to result directly from such advertising. However, under View A, including the direct-response advertising as part of DAC would subject those costs to a premium deficiency model that does not include expected revenues and could therefore result in impairment. Supporters of View A believe that while this argument has conceptual merit, there are few property and casualty insurers that are currently capitalizing direct-response advertising outside of DAC, and therefore believe the effect of View A would be minimal.

*View B: Perform the realizability of direct-response advertising analysis first and then perform the premium deficiency analysis by adding the carrying amount of any direct-response advertising to the amount of unamortized acquisition costs included in the premium deficiency calculation.*

22. Proponents of View B believe that insurance entities should perform the realizability test for direct-response advertising first, followed by their premium deficiency analysis. Assuming that the direct-response realizability analysis does not yield an impairment of the entire amount of direct-response advertising, the insurance entity would add any remaining carrying amount of its

direct-response advertising to the amount of unamortized acquisition costs in its premium deficiency analysis as noted in the following illustrations:

*Short-Duration Contracts*

| | Current Method | View B Method |
|---|---|---|
| Expected claim costs | 100 | 100 |
| Claim adjustment expenses | 25 | 25 |
| Expected dividends to policyholders | 10 | 10 |
| Unamortized acquisition costs | 50 | 50 |
| **Unamortized direct-response advertising costs** | **N/A** | **75** |
| Maintenance costs | 15 | 15 |
| | 200 | 275 |
| Unearned premiums | 250 | 250 |
| Premium Surplus / (Deficiency) | 50 | (25) |

23. In the short-duration contract example above, the entity first performed its realizability test for direct-response advertising first, and noted no impairment. Therefore, the entity added the entire carrying value ($75) of direct-response advertising in its premium deficiency analysis, which resulted in a premium deficiency. The recognition of premium deficiencies will be addressed later in this memorandum.

*Long-Duration Contracts*

| | |
|---|---|
| Present value of future payments for benefits and related settlement and maintenance costs, determined using revised assumptions based on actual and anticipated experience | 125 |
| Less the present value of future gross premiums, determined using revised assumptions based on actual and anticipated experience | 350 |
| Liability for future policy benefits using revised assumptions | 225 |
| Less the liability for future policy benefits as the valuation date, reduced by unamortized unamortized acquisition costs and | 50 |
| **unamortized direct-response advertising costs** | 75 |
| Premium Surplus / (Deficiency) | 100 |

24. In the long-duration contract example above, the entity first performed its realizability test for direct-response advertising first, and noted no impairment. Thus, the entity added the entire carrying value ($75) of direct-response advertising in its premium deficiency analysis, which did not result in a premium deficiency. Therefore, the entity was able to demonstrate that both the unamortized acquisition and direct-response advertising assets were recoverable. However, if the application of this methodology resulted in a premium deficiency, it would be recognized in the manner described later in this memorandum.

25. Proponents of View B believe that this methodology provides preparers with a reasonable approach for supporting the recoverability of the direct-response advertising. However, View B proponents also acknowledge that the amortization periods of direct-response advertising and unamortized acquisition costs may be different, thus skewing the premium deficiency analysis.

*Impairment Recognition*

26. The staff believes that the recognition of any premium deficiency resulting from the methodology proposed in View A would continue to follow the guidance in paragraphs 944-60-25-5 through 25-6 and 944-60-25-8. That is, for short-duration contracts, a premium deficiency shall first be recognized by charging any unamortized acquisition costs to expense to the extent required to eliminate the deficiency. If the premium deficiency is greater than the unamortized

acquisition costs, a liability shall be accrued for the excess deficiency. For long duration contracts, the premium deficiency shall be recognized by a charge to income and either of the following:

a. A reduction of unamortized acquisition costs
b. An increase in the liability for future policy benefits.

27. The staff also believes that if the methodology in View B is selected by the Task Force, the methodology used to recognize any premium deficiency would need to be adjusted for both short-duration and long-duration contracts. The staff believes that for short-duration contracts, a premium deficiency shall first be recognized by charging any unamortized acquisition costs to expense to the extent required to eliminate the deficiency. If the premium deficiency is greater than unamortized acquisition costs, any unamortized direct-response advertising costs would be charged to expense to the extent required to eliminate the deficiency. If the premium deficiency is greater than the unamortized acquisition costs and the unamortized direct-response advertising costs, a liability shall be accrued for the excess deficiency. For long duration contracts, the premium deficiency shall be recognized by a charge to income and either of the following:

a. A reduction of unamortized acquisition costs
b. A reduction of unamortized direct-response advertising costs
c. An increase in the liability for future policy benefits.

**Issue 2: What the transition method should be for this Issue.**

28. The amendments in the proposed Update permit early adoption and require prospective application upon the date of adoption. Additionally, retrospective application to all prior periods upon the date of adoption is also permitted, but not required. In addition to the transition methods contained in the proposed Update, the staff believes that there are additional transition options that the Task Force should consider. Each of the transition methods as well as additional staff analysis is presented in the following paragraphs.

*View A: Require prospective application. Additionally, retrospective application to all prior periods would be permitted, but not required.*

29. Supporters of View A believe that requiring prospective application is appropriate given the potential difficulty for some preparers in obtaining the historical data needed to comply with the proposed guidance. These proponents also believe that requiring retrospective application to all prior periods upon adoption would not be practicable in some cases. View A supporters also believe that because of the current diversity in practice regarding what gets capitalized into DAC, insurance entities may be impacted differently depending on their prior policies, which may affect their decision about whether it would be worth the effort to apply the proposed Update retrospectively. Thus, proponents of View A believe that this transition method would reduce the costs and complexities associated with accumulating and analyzing historical data for a number of prior periods, as would likely be the case for life insurance entities, in order to be able to retrospectively apply the proposed guidance. However, View A supporters do not want to preclude entities that have the ability to retrospectively adopt the proposed Update from doing so, mainly because retrospective application is generally favored by users of the financial statements.

*View $A^1$: Require prospective application. Additionally, retrospective application to all prior periods would not be permitted.*

30. Supporters of View $A^1$ agree with proponents of View A that requiring prospective application is appropriate given the potential difficulty for some preparers in obtaining the historical data needed to comply with the proposed guidance. However, these proponents are not in favor of permitting an option to apply the proposed Update retrospectively because they believe that all entities should apply the guidance in the same way for comparability purposes.

*View B: Require retrospective application to all prior periods, unless the entity determines that it is impracticable to do so.*

31. View B supporters are in favor of requiring retrospective application and believe that this transition method would be the preferred method of some life insurance entities. However, View B supporters acknowledge that retrospective application would only be possible for some insurance entities if they were able to use a level of estimation that would be considered "practicable" under existing accounting standards because the historical records necessary to apply the guidance retrospectively may not exist.

*Staff Analysis*

32. As noted in the Working Group Report, the Working Group discussed whether requiring prospective application as well as requiring additional disclosures that would give users the information needed to evaluate comparability of the current period to prior periods would be a possible approach. Some Working Group members stated that if companies were required to disclose a "best guess" of what DAC would have been in prior periods, it would be preferable if estimates were used for retrospective application rather than only for disclosure, even if those estimates were determined using a practical expedient.

33. The staff examined whether a practical expedient could be created to allow for retrospective application in the case of a lack of historical data, and looked to existing accounting literature for examples of practical expedients used in the adoption of new accounting standards. The staff could not identify any examples of practical expedients that have been used in the adoption of new accounting standards. One method that was suggested by the Working Group was to allow insurance entities to use the information gathered in the current period to comply with the proposed model and apply that information to historical periods. Specifically, insurance entities would use the time studies prepared in the current period and extrapolate the results of those studies to their historical data to create comparable information for the prior periods for which historical data was not available.

34. The staff also examined International Financial Reporting Standard 1, *First-time Adoption of International Financial Reporting Standards*, to determine whether there are any practical expedients that could be analogized to for this situation. The staff noted that IFRS 1 grants

limited exemptions in specific areas where the cost of complying with the adoption requirements would likely exceed the benefits to users of the financial statements. However, these exemptions were not the equivalent of practical expedients. That is, the exemptions in the standard provide preparers with flexibility in having to comply with certain aspects of various accounting requirements upon adoption rather than providing preparers with simplified methods of implementing accounting requirements.

35. Lastly, the staff performed outreach to users of insurance company financial statements. Specifically, the staff asked a number of users whether they would be supportive of the use of a practical expedient to aid in the transition of the proposed standard. Specifically, the staff asked users if the retrospective transition method was used, whether a practical expedient such as using the information gathered in the current period as a proxy and applying that information to historical periods would be preferable to prospective application. Said differently, would users rather have historical information recast using recent period data as the basis for recasting that information even if the recasted information may not be reflective of what results would have been had the new guidance been applied in those prior periods?

36. The results of the user outreach were mixed. The staff received comments from three users of insurance entity financial statements. One of the users did not believe that retrospectively applying a standard with data that is not reflective of the actual results of the prior periods would provide useful information for analysts. Another user said that they would prefer to see retrospective application, but could live with the practical expedient measure discussed in the previous paragraph. The remaining user did not have a strong preference either way. The staff believes that using recent information as a practical expedient for estimating the effects in prior periods may not be reflective of the actual results for those prior periods because of the abnormal market activity that has occurred in recent years. Additionally, the staff believes that historical changes in the entity's business practices would further complicate the application of this type of practical expedient. Thus, the staff does not recommend that the Task Force utilize this approach.

37. As noted by some Working Group members, retrospective application will likely require some level of estimation that companies and their auditors will need to assess to determine whether the use of those estimates produces results that are reasonably stated using the new model. A significant consideration in determining the reasonableness of relying on those estimates is an individual entity's materiality level. In the staff's view, retrospective application should only be permitted if the resulting information would be reasonably stated in all material respects. Using a practical expedient does not provide sufficient assurance that information is materially correct and could potentially be misleading. In addition to assessing materiality, applying the proposed Update retrospectively would be further complicated by historical changes in the level of operations and activity, changes in distribution channels, changes in cost structure, reorganizations, and so forth. Accordingly, the staff believes that if the Task Force decides to require retrospective application, the guidance in Subtopic 250-10 should be applied. The application of that guidance may result in some entities determining that it is impracticable to apply retrospectively if materially supportable estimation techniques are not available to them.

38. However, the staff also acknowledges that although there is not a specific practical expedient that entities could apply in all circumstances, it is expected that companies would need to make reasonable estimates of the impact on prior years based on their specific circumstances, and are not necessarily expected to go back and redo their detailed capitalization, amortization, and premium deficiency calculations for every prior year if they have ways to reasonably estimate those numbers in accordance with Subtopic 250-10.

**Issue 3: The quantitative disclosures that should be required to communicate the effect of the change from adopting the proposed Update if the Task Force chooses (a) retrospective transition or (b) prospective transition.**

39. The guidance in Subtopic 250-10 is applicable for any change in accounting principle, including a change in the method of applying an accounting principle. An informal comment was received relating to how the Task Force intended entities to comply with the following disclosure requirement in paragraph 250-10-50-1b(2):

> The effect of the change on income from continuing operations, net income (or other appropriate captions of changes in the applicable net assets or performance indicator), any other affected financial statement line item, and any affected per-share amounts **for the current period** and any prior periods retrospectively adjusted.

40. The commenter observed that this disclosure requirement would require an entity to maintain two sets of books during the year of adoption regardless of whether adoption was through prospective or retrospective application. The commenter questioned the cost-benefit of that disclosure. In response to that comment, the staff has prepared the following views for the Task Force to evaluate as potential transition disclosures to describe the effect of the change. Different transition requirements may be required depending on whether the guidance is adopted retrospectively or prospectively. Views A and B should be considered for retrospective adoption while all views should be considered if transition is prospective.

*View A: Require the disclosure of the effect of the change on the current period as required by paragraph 250-10-50-1b(2).*

41. Proponents of View A believe that disclosure of the effect of the change on recent periods is needed to provide more transparent trend information in order for users to be able to assess the effect of the change on future periods. Proponents of View A believe that this trend information is even more critical when prospective transition exists because there is no comparative data provided to understand how the change affected the entity's results. Some View A proponents also believe this information is useful even when retrospective transition has been applied because it provides the most up-to-date information for investors to analyze trends.

*View B: Do not require disclosure of the effect of the change in the current period as noted in paragraph 250-10-50-1b(2).*

42. Proponents of View B do not believe that the benefits provided by disclosing the effect of the change offset the costs of maintaining two sets of records during the period of adoption. Those proponents believe that this is especially true when retrospective application has been applied since recent trend information does exist. If transition is prospective, proponents of

View B believe that qualitative disclosure of the effect of the change could be provided in order for investors to understand how the change would likely affect the entity's results.

*View C: Require entities to disclose either of the following in lieu of the disclosure of the effect of the change on the current period in paragraph 250-10-50-1b(2):*

*a. The amount of acquisition costs that would have been capitalized during the corresponding period immediately preceding adoption as if the guidance in the proposed Update had been applied during that period compared to the amount previously capitalized during that period.*

*b. The amount of acquisition costs capitalized during the period of adoption compared to the amount of acquisition costs that would have been capitalized during the period if the entity's previous policy had been applied during that period.*

43. Proponents of View C believe that providing at least one period of comparative information about how the change in accounting affected the amount of cost that was capitalized provides sufficient information to investors about how the change affected the entity. Proponents of View C note that this transition adoption is similar to that required in Update No. 2009-13 *Revenue Recognition (Topic 605): Multiple-Deliverable Revenue Arrangements* (EITF Issue No. 08-1, "Revenue Arrangements with Multiple Deliverables") and Update No. 2009-14 *Software (Topic 985): Certain Revenue Arrangements That Include Software Elements* (EITF Issue No. 09-3, "Applicability of AICPA Statement of Position 97-2 to Certain Arrangements That Include Software Elements"). Proponents of View C would give entities the option of providing this disclosure for either the period of change or the period immediately preceding the change to provide entities with the choice of whether to maintain two sets of records during the adoption period. These proponents note that many entities may go through an analysis of previous period costs while preparing to implement the standard and, therefore, may be able to provide that information more easily than if they had to continue maintaining two sets of records.

**Issue 4: Whether the Task Force agrees with the staff recommendation to defer the effective date of the proposed Update to fiscal years, and interim periods within those fiscal years, beginning after December 15, 2011.**

44. As exposed, the amendments in the proposed Update would be effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2010.

*Staff Analysis and Recommendation*

45. The general consensus of Working Group members was that meeting the effective date of the proposed Update would be a challenge, at best. The staff agrees with Working Group members who believe that there could be significant system changes and implementation challenges primarily related to the distinction between successful and unsuccessful contracts. Additionally, the staff and Working Group members believe that there will be a significant amount of time necessary to generate reliable time studies to capture information about successful and unsuccessful efforts.

46. As a result of the feedback provided by the Working Group, the staff supports a deferral of the effective date of the proposed Update and believes that the Issue should be effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2011. The staff believes that deferring the proposed effective date for one year will provide insurance entities with sufficient time to implement the requirements of the proposed Update and to complete any necessary time studies or cost analyses, make requisite system changes, and update their internal control processes to integrate any changes into their pre-existing DAC internal controls.

**Issue 5: Whether the Task Force agrees with the staff's drafting changes to the amendments to the Codification.**

47. The staff has made several drafting changes to the amendments to the Codification related to the proposed Update since it has been exposed. Those changes are highlighted in the updated draft of the Codification amendments attached as Appendix 09G-B. Most of the changes are editorial in nature; however, the staff would like to highlight that the amendments have been updated to reflect the Task Force tentative conclusion from the March 18, 2010 meeting, that entities should not be required to capitalize additional costs as a result of applying the guidance

in the proposed Update. The staff understands that this decision was provided for cost-benefit reasons so that entities that had not previously been capitalizing certain costs under their policy of applying the "vary with and primarily related to" guidance would not have to incur additional costs to begin analyzing those costs for capitalization under the new model. The staff believes that this exception would most likely apply to property and casualty companies, particularly if they had previously only been capitalizing commissions and premium taxes.

48. The staff also modified the Codification amendments in response to a Task Force member comment made at the March 18, 2010 EITF meeting. That Task Force member thought the language used in the proposed Update to define incremental direct costs of contract acquisition, which specifically requires that a cost "would not have been incurred by the insurance entity if the contract had not been acquired," was inconsistent with an example of an incremental direct cost provided in the implementation guidance (i.e. a third-party medical or inspection fee for a successful contract acquisition). The Task Force member believed that this example was inconsistent because a third-party medical cost would likely be incurred prior to determining whether a contract was successful, and thus would not meet the definition of "a cost that would not have been incurred by the entity if the contract has not been acquired." The staff agreed with this comment and removed the example from the implementation guidance. However, the staff also believes that third-party medical costs would be capitalizable under the proposed Update and would be an example of an "other cost related to those activities that would not have been incurred if the contract had not been acquired."

49. The staff also changed the terminology used to describe one of the activities for which an employee's total compensation and payroll-related fringe benefits directly related to time spent performing the activity would be capitalizable from "Contract Selling" to "Sales Force Contract Selling." The staff made this change to clarify its original intention that an employee's total compensation and payroll-related fringe benefits directly related to time spent performing selling activities by an insurer's sales force and/or agents that result in successful contract acquisitions would be capitalizable. The staff believes that the original wording was too broad and could be misinterpreted in practice and believes that the revised language clarifies its intent.

50. Lastly, the staff added paragraph 944-30-25-1(c), "Other costs related to those activities that would not have been incurred if the contract had not been acquired," as a conforming change. That sentence was used in the Summary section of the proposed Update, but was not included in the Codification amendments of the proposed Update. Thus, the staff included the language in the revised Codification amendments to reflect the Task Force's original intent and to be consistent with the language in the proposed Update.

**Appendix 09G-A**

## EITF Issue 09-G Working Group Report

**Issue No.** 09-G

**Title:** Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts

**Document:** Working Group Report No. 1*

**Date prepared:** June 7, 2010

**FASB Staff:** Brower (ext. 468) / Bonn (ext. 226)

**EITF Liaison:** Mark Bielstein

**Dates previously discussed:** November 19, 2009; March 18, 2010

**Previously distributed EITF materials**: Issue Summary No. 1, dated November 5, 2009; Issue Summary No. 1, Supplement No. 1, dated March 4, 2010

### Background

1. At the March 18, 2010 EITF meeting, the Task Force affirmed its consensus-for-exposure that acquisition costs should include only those costs that are directly related to the acquisition or renewal of insurance contracts by applying a model similar to the accounting for loan origination costs in Subtopic 310-20. The Task Force also affirmed its consensus-for-exposure that costs related to unsuccessful contract efforts should be expensed as incurred and that advertising costs should only be capitalized if the criteria for capitalizing such costs pursuant to the direct-response advertising guidance in Topic 340 are met.

2. The Task Force also discussed concerns raised by comment letter respondents relating to the costs and efforts involved in implementing the proposed model. Those respondents frequently cited system costs associated with the identification and allocation of costs between successful

* **The alternative views presented in this Working Group Report are for purposes of discussion by the EITF. No individual views are to be presumed to be acceptable or unacceptable applications of Generally Accepted Accounting Principles until the Task Force makes such a determination, exposes it for public comment, and it is ratified by the Board.**

and unsuccessful efforts as a complicating factor in implementing the model. As a result, the Task Force requested that the staff perform additional research on the efforts required and methodologies that could be used to implement the proposed model. As such, the Task Force deferred discussion on the effective date and transition methods of the proposed guidance pending the outcome of the staff's research.

3. In response to the Task Force's request, the EITF Issue 09-G Working Group (the Working Group) was formed. The Working Group included preparers and auditors of life insurance and property and casualty insurance entities, a life insurance industry association representative, and an observer from the Securities and Exchange Commission. Additionally, several Task Force members observed and participated in the meeting, which was held on May 13, 2010. The paragraphs that follow summarize the discussions of the Working Group, and are being provided to the Task Force for its consideration as it deliberates the effective date and transition methods of the proposed model.

**Working Group Discussion**

4. The initial questions posed to the Working Group by the staff focused on the identification of capitalizable acquisition costs under the proposed model. The staff asked Working Group members to identify the level at which they expected preparers will track acquisition costs to properly apply the requirements of the proposed model (for example, portfolio, product, cohort, individual contract, or other). One Working Group member suggested that, for life insurers, costs are currently commonly captured by product type for a particular issue year (commonly referred to as a "cohort"). The general consensus among Working Group members was that preparers could utilize existing cost pools in some cases to identify costs that would be capitalizable under the proposed model and would not have to drill down to the most granular level (that is, the contract level) to comply with the proposed model. However, Working Group members acknowledged that in many cases there could be entities for which it will be necessary to track acquisition costs at a lower level than is currently being used to track acquisition costs. This is because the current cohort approach does not consider differences in underwriting efforts that may relate to a given product or different success rates for similar underwriting efforts that may occur in different operational areas. Some Working Group members also cited operational

issues associated with determining when an effort is considered successful versus unsuccessful. For example, that member thought it may be challenging to determine how many contracts are "successful" in the case of a large commercial account that has multiple contracts that are sold in bundles.

5. Working Group members also commented that the level of difficulty in implementing the proposed model would depend on the nature of the underlying acquisition effort. As such, Working Group members believe that there would likely need to be some level of aggregation and allocation of costs, and that contract-by-contract tracking of costs would rarely be feasible. One Working Group member highlighted a similar transition that occurred when financial institutions initially applied the requirements of FASB Statement No. 91, *Accounting for Nonrefundable Fees and Costs Associated with Originating or Acquiring Loans and Initial Direct Costs of Leases*. For example, that member stated that for some financial institutions first applying Statement 91, costs were allocated to loans that were aggregated into pools until their information systems were ready to track and accumulate costs on a loan-by-loan basis. Thus, the member believes that the insurance industry could follow a similar path.

6. Working Group members discussed whether isolating and accounting for acquisition costs that are in-process (that is, the point in the new or renewal contract acquisition process when it is unclear whether the efforts will result in a successful contract) will be a complex task. Members of the Working Group noted that acquisition efforts may occur over extended periods of time (for example, when negotiating a contract with a large commercial client) and, therefore, estimation methods will be necessary to determine what portion of the in-process costs would result in a successful effort and therefore be eligible for deferral.

7. The staff also asked Working Group members whether they believe preparers would need to track actual acquisition costs or whether standard costing or other systems could be utilized. Members of the Working Group stated that some life insurance companies are currently using quasi-standard costing systems and that even in a fully standard costing system, preparers would periodically need to assess whether their standard costs approximated actual costs. Other

Working Group members stated that the feasibility of using a standard costing system would depend on the type of insurance product being sold and how certain costs would be allocated.

8. Working Group members also discussed whether there would be new information that preparers will need to accumulate in order to comply with the proposed model. While some Working Group members indicated that information related to unsuccessful efforts (for example, declined applications) may exist in certain cases, the Working Group indicated that many companies may not have captured that information on a historical basis. Others stated that even if information about accepted/rejected applications has been captured, information about the costs associated with accepting or rejecting those applications is rarely captured. Still others indicated that any information historically captured may have been done for operational reasons using systems and processes that were not considered part of the financial reporting system and, therefore, would not have been subject to audit verification and Sarbanes-Oxley (SOX) procedures.

9. Some Working Group members stated that significant time and effort would be required to generate reliable and auditable time studies to capture information about successful and unsuccessful efforts. One Working Group member stated that, in general, it takes approximately six months to complete a time study, although the length of time may vary by type of product because the underwriting/acquisition effort may vary by product. However, given the challenge of distinguishing successful efforts from unsuccessful efforts, some Working Group members believe that a longer period will be required to complete those studies, particularly due to the time necessary for preparers to validate the success rates of new or renewal contract acquisitions. Those Working Group members also believe that this analysis would be further complicated because it is likely that there will be a different renewal cycle for certain types of products and the types of businesses that are being insured (that is, each product has its own distinct renewal cycle that will affect the success of an application). For example, some contract signings or renewals are concentrated at particular times of the year and companies would likely want to complete their time study for those types of contracts, if significant, at those times of the year. Additionally, the length of time needed for the acquisition effort may vary by product. For example, a particular product may be underwritten almost immediately, while another requires

more extensive consideration of various factors. Finally, one Working Group member cited that time studies from the current year might provide more "normalized" data whereas studies from the past couple of years would be abnormally volatile for the industry as a result of the financial crisis. Even if such historical data is available for the time studies, it may not provide an accurate picture of the acquisition efforts of the organization during the current period.

10. Working Group members were then asked whether they thought that system changes would be required in order to implement the requirements of the model. Some Working Group members stated that some systems currently capture the total number of applications received (including how many are accepted or rejected), but do not track the amount of time spent on each application, or the amount of time that it takes to determine whether an application will be successful and will therefore require modification. Additionally, Working Group members believe that global and more complex organizations that are implementing the proposed model may require more than one system to be changed. For example, an insurance company that has increased in size as a result of numerous acquisitions may be utilizing a number of information systems that would have to be changed in order to comply with the requirements of the proposed model. Likewise, an insurer that employs multiple distribution systems or uses more than one underwriting process may have to modify several systems to capture data related to unsuccessful efforts.

11. Working Group members also believe that changing systems, particularly late in the year, could have SOX and external audit implications. The various system changes would need to be analyzed over the renewal cycle by management to determine whether the information coming out of those systems is accurate. Additionally, some of the non-financial systems used to capture newly-required data elements could possibly be generated from non-SOX-compliant systems (for example, informal spreadsheets used to track volume of application data), requiring additional documentation and testing by management followed by additional testing by the external auditor.

12. Working Group members also discussed whether they thought that insurance entities may change their business models or compensation plans as a result of the proposed guidance on acquisition costs. One Working Group member noted that there may be some compliance areas

that could be tied more closely to contracts and possibly be associated with successful and unsuccessful contracts, while another Working Group member stated that their business practices would not change as a result of the proposed guidance, particularly given the potential significant changes forthcoming in the Board's insurance project. Another Working Group member stated that any changes in compensation arrangements that may result are business decisions rather than accounting decisions. One Working Group member also stated that insurance entities are being approached by third parties to perform services that would be capitalizable under the proposed model if the functions were outsourced as opposed to being conducted internally.

13. The Working Group also discussed the Task Force's proposal that entities should not be required to capitalize more acquisition costs under the proposed model than they already have been capitalizing under the current model. The Task Force had proposed this option as a practical consideration to allow entities that were capitalizing only incremental costs to avoid investing time and money in system changes only to have to switch to expensing all acquisition costs as a result of the conclusions in the Boards' joint project on insurance contracts.

14. Working Group members debated whether they thought that decision would reduce consistency and comparability between financial statements. During the discussion, one Working Group member asked whether the proposed model was intended to be contract category-specific or whether the model only applied to the full amount of capitalized acquisition costs for an entity. For example, some insurance entities have multiple lines of business (that is, both life insurance and property and casualty insurance) and might have an increase in capitalization in the property and casualty category, but an overall decrease in cost capitalization because of reduced capitalization in the life insurance business. That Working Group member suggested that some entities may be interested in an option to stop capitalizing underwriting, policy issuance, and similar allocated costs even if overall costs to be capitalized under the proposed guidance were not in excess of historical amounts capitalized, because they would rather expense those other costs than incur the costs necessary to make the system changes required to comply with the proposed guidance. Some Working Group members believe that allowing this type of option to capitalize only certain costs would increase diversity and reduce the comparability of financial statements and were not in favor of permitting the optionality.

15. The Working Group then discussed the potential effective date and transition methods of the proposed guidance. The general consensus of Working Group members was that meeting the effective date (for fiscal years beginning on or after December 31, 2010) would be "difficult at best." One Working Group member commented that the insurance entities estimated that it would take between 6 and 18 months to implement a SOX-compliant proposed model and would be particularly difficult for global or more complex organizations. That Working Group member thought the implementation challenges primarily related to the distinction between successful and unsuccessful contracts, rather than limiting the types of costs that could be capitalized.

16. In the proposed guidance, the Task Force proposed a transition that required prospective application but allowed for retrospective application, if practical. During the discussion, some Working Group members thought that some insurers (particularly life insurers) would favor requiring retrospective application. However, those Working Group members also thought that retrospective application would only be possible if insurance entities used some level of estimation that would be considered "practicable" under existing accounting standards. Another Working Group member stated that they would prefer that all companies apply the guidance in the same way (that is, they would prefer that any optionality in transition methods be eliminated). The Working Group also discussed whether a practical expedient to allow for retrospective application could be created because some entities have concerns about retrospective application because it is likely they will not have the historical data to support adopting the standard retrospectively. Another Working Group member stated that starting with current year figures and using extrapolation as a practical expedient could be a potential solution, while another Working Group member suggested looking to IFRS 1, *First-time Adoption of International Financial Reporting Standards*, to see if there are any practical expedients that could be analogized to for this situation. Other Working Group members noted that using recent trends as a proxy for estimating the effect for prior periods may not be reflective of the actual results for those prior periods because of the abnormal market activity during the past two years.

17. The Working Group discussed what would happen if the Task Force required prospective application and whether there might be disclosures that would give users the information needed

to evaluate comparability of the current period to prior periods. One Working Group member suggested that companies could disclose a "best guess" of what DAC would have been in prior periods, but preferred that if estimates were going to be used that they be used for retrospective application rather than only for disclosure.

18. The staff then asked the Working Group whether it would be possible for the Board to require insurance entities to expense acquisition costs ahead of the effective date of the Boards' joint project on insurance contracts and whether the conclusion to expense acquisition costs would impact other aspects of the current insurance accounting model. One Working Group member replied that a decision to expense DAC now would not be appropriate because DAC is one part of the current liability measurement model, and the expensing of DAC should only be considered in the context of a reevaluation of the measurement of the overall liability within the context of the existing conceptual insurance accounting model. Other Working Group members noted that allowing an option to expense all acquisition costs would not reduce diversity in practice.

19. Lastly, the Working Group suggested that the staff update the Task Force on the progress made to date on the Boards' joint project on insurance contracts at the upcoming EITF meeting. Additionally, the Working Group suggested that the staff perform additional outreach to users to determine whether they prefer any particular transition method over another and to provide the results of that outreach to the Task Force as well.

**Appendix 09G-B**

# Amendments to the *FASB Accounting Standards Codification*™

## Introduction

1. The Accounting Standards Codification is amended as described in paragraphs 2–12. In some cases, not only are the amended paragraphs shown but also the preceding and following paragraphs are shown to put the change in context. Terms from the Master Glossary are in **bold** type. Added text is underlined and deleted text is ~~struck out~~.

## Amendments to Subtopic 944-30

### Financial Services—Insurance—Acquisition Costs

2. Amend Master Glossary term *Acquisition Costs,* with a link to transition paragraph 944-10-65-1, as follows:

**Acquisition Costs**

~~Costs incurred in the acquisition of new and renewal insurance contracts.~~ A cost~~Acquisition costs include those costs~~ that ~~vary with and are primarily~~ is directly related to the successful acquisition of a new or renewal insurance ~~contracts.~~ contract.

3. Add the term *Incremental Direct Cost of Contract Acquisition* to the Master Glossary, with a link to transition paragraph 944-10-65-1, as follows:

**Incremental Direct Cost of Contract Acquisition**

A cost that has both of the following characteristics:

a. It results directly from the acquisition of the contract
b. It would not have been incurred by the insurance entity had the contract not been acquired.

4. Add new paragraph 944-30-25-1, with a link to transition paragraph 944-10-65-1, as follows:

### Recognition

**944-30-25-1** An insurance entity shall capitalize only ~~both of~~ the following as acquisition costs:

a. Incremental direct costs of contract acquisition (for implementation guidance, see paragraph 944-30-55-1)
b. The portion of the ~~insurance entity~~ employee's total compensation and payroll-related fringe benefits directly related to time spent performing any of the following acquisition activities for a contract that has actually been acquired:
   1. Underwriting
   2. Policy issuance and processing
   3. Medical and inspection
   4. ~~Contract~~ Sales force contract selling.
c. Other costs related to those activities that would not have been incurred if the contract had not been acquired.

5. Amend existing paragraph 944-30-25-1 and renumber as paragraph 944-30-25-1A, with a link to transition paragraph 944-10-65-1, as follows:

**~~944-30-25-1~~944-30-25-1A** ~~**Acquisition costs** shall be capitalized.~~ To associate such costs with related premium revenue, capitalized acquisition costs shall be allocated by groupings of insurance contracts consistent with the entity's manner of acquiring, servicing, and measuring the profitability of its insurance contracts.

6. Add new paragraph 944-30-25-1B, with a link to transition paragraph 944-10-65-1, as follows:

**944-30-25-1B** An insurance entity shall not include advertising costs as acquisition costs. For guidance on accounting for advertising costs, see Subtopics 720-35 and ~~Subtopic~~ 340-20.

7. Amend existing paragraph 944-30-25-2, with a link to transition paragraph 944-10-65-1, as follows:

**944-30-25-2** Paragraph 944-720-25-2 requires that an insurance entity expense, as incurred, certain other ~~costs~~costs. ~~incurred during the period—such as those relating to investments, general administration, and policy maintenance—that do not vary with and are not primarily related to the acquisition of new and renewal insurance contracts shall be charged to expense as incurred.~~

8. Amend paragraph 944-30-50-1 and its related heading, with a link to transition paragraph 944-10-65-1, as follows:

## Disclosure

**944-30-50-1** Insurance entities shall disclose all of the following in their financial statements:

a. The nature and type of **acquisition costs** capitalized
b. The method of amortizing capitalized acquisition costs
c. The amount of acquisition costs amortized for the period.

9. Amend paragraph 944-30-55-1, with a link to transition paragraph 944-10-65-1, as follows:

## Implementation Guidance and Illustrations

### > Implementation Guidance

### >> ~~Acquisition Costs~~Incremental Direct Costs of Contract Acquisition

**944-30-55-1** ~~All of the following costs vary with and are primarily related to insurance contracts issued or renewed during the period in which the costs are incurred and shall be considered **acquisition costs**:~~~~This implementation guidance provides examples of~~ Paragraph 944-30-25-1(a) requires that an insurance entity capitalize incremental direct costs of contract acquisition. Such costs include, ~~both of~~ but are not limited to, the following:

a. ~~Agent and broker commissions~~An agent or broker commission or bonus for a successful contract acquisition
b. Subparagraph superseded by Accounting Standards Update 2010-XX.~~Salaries of certain employees involved in the underwriting and policy issue functions~~
c. ~~Medical and inspection fees.~~~~A third-party medical or inspection fee for a successful contract acquisition.~~

10. Amend paragraphs 944-720-25-1 through 25-2, with a link to transition paragraph 944-10-65-1, as follows:

## Financial Services—Insurance—Other Expenses

### Recognition

**944-720-25-1** Paragraph 944-30-25-1 ~~states that costs that are~~ requires that an insurance entity capitalize certain **acquisition ~~costs~~costs**. ~~shall be capitalized.~~

**944-720-25-2** ~~Other costs incurred during the period—such as those relating to investments, general administration, policy maintenance, product development expenses, market research expenses, and general overhead—that do not vary with and are not primarily related to the acquisition of new and renewal insurance contracts shall be charged to expense as incurred.~~An insurance entity shall expense, as incurred, any of the following costs:

a. An acquisition-related cost not capitalizable in accordance with paragraph 944-30-25-1 (for implementation guidance, see paragraph 944-720-55-1)
b. An indirect cost (for implementation guidance, see paragraph 944-720-55-2).

11. Add paragraphs 944-720-55-1 through 55-2 and their related headings, with a link to transition paragraph 944-10-65-1, as follows:

**> Implementation Guidance**

**> > Certain Acquisition-Related Costs**

**944-720-55-1** This implementation guidance addresses paragraph 944-720-25-2(a), which requires that an insurance entity expense, as incurred, any acquisition-related cost not ~~identified~~capitalizable in accordance with paragraph 944-30-25-1. Such costs include, but are not limited to, costs of all of the following:

a. Soliciting potential customers
b. Market research
c. Training
d. Administration
e. Unsuccessful acquisition or renewal efforts
f. Product development.

**> > Indirect Costs**

**944-720-55-2** This implementation guidance addresses paragraph 944-720-25-2(b), which requires that an insurance entity expense, as incurred, any indirect cost. Such costs include, but are not limited to, all of the following:

a. Administrative costs
b. Rent
c. Depreciation
d. Occupancy costs
e. Equipment costs
f. Other general overhead.

12. Add paragraph 944-10-65-1 and its related heading as follows:

**> Transition Related to Accounting Standards Update No. 2010-XX, *Financial Services—Insurance (Topic 944): Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts***

**944-10-65-1** The following represents the transition and effective date information related to Accounting Standards Update No. 2010-XX, *Financial Services—Insurance (Topic 944): Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts:*

a. An entity shall apply the pending content that links to this paragraph either:
   1. ~~On a~~ Prospectively ~~basis~~ in fiscal years beginning after December 15, 2011, and interim periods within those fiscal years
   2. ~~On a~~ Retrospectively ~~basis~~ to all prior periods.
b. Earlier application of the pending content that links to this paragraph is permitted.
c. An entity shall provide the disclosures in paragraphs 250-10-50-1 through 50-3 in the period the entity adopts the pending content that links to this paragraph.
d. If the application of the guidance in paragraph 944-30-25-1 would result in the capitalization of acquisition costs that had not previously been capitalized by the entity, the entity may elect not to capitalize those types of costs.