MINUTES

Financial Accounting Standards Board

To:	Board Members
From:	Insurance Contracts Team (Jones, ext. 384)
Subject:	Minutes of the June 23, 2010, Joint Board Meeting: Insurance Contracts
Date:	July 2, 2010
cc:	FASB: Bielstein, Golden, Stoklosa, Chookaszian, Posta, Guasp, Sutay, Klimek, Gabriele, McGarity, Proestakes, Cropsey, Lott, Hood, Brickman, Galloway (GASB), FASB Intranet; IASB: Leisenring, Clark, van der Veen, Hack, Jordan, Teixeira

The Board meeting minutes are provided for the information and convenience of constituents who want to follow the Board's deliberations. All of the conclusions reported are tentative and may be changed at future Board meetings. Decisions become final only after a formal written ballot to issue a final Accounting Standards Update.

Topic:	Insurance Contracts— Cash flows, unbundling, presentation, and interest accretion
Basis for Discussion:	Board Memorandum Nos. 51 through 51G
Length of Discussion:	9:00 a.m. to 12:35 a.m. (EST)

Attendance:

Board members present:	FASB: Herz, Smith, Siegel, Seidman and Linsmeier (via video)
	IASB: Tweedie, Cooper, Engström, Smith (by phone), Wei-Guo (by phone), Danjou, Gomes, Kalavacherla, Mcgregor, Yamada (by video), McConnell

Board member absent:	Leisenring, Finnegan, Garnett, and Gelard
Staff in charge of topic:	van der Veen
Other staff at Board table:	IASB: Clark, Hack, d'Eri, and Upton (by phone)
Staff participating by video:	FASB: Golden, Cropsey, Trench, Proestakes, Jourdan, Brickman, and Jones

Type of Document and Timing Based on the Technical Plan:

The Board met to discuss issues relating to the development of an Exposure Draft addressing insurance contracts.

Please refer to the current technical plan for information about the expected release dates of exposure documents and final standards.

Summary of Decisions Reached:

At this meeting the Boards discussed:

1. Cash flows, including acquisition costs and participating contracts
2. Follow-up on unbundling
3. Presentation of the statement of comprehensive income
4. Interest accretion for residual and composite margins.

Cash Flows

The Boards decided tentatively that the measurement of a portfolio of insurance contracts should include the expected present value of the incremental cash flows arising from that portfolio. In addition, the cash flow guidance will clarify:

1. That, at initial recognition, the measurement will include all cash flows arising from the existing contracts over the lives of those contracts. For subsequent reporting periods, the measurement will include the remaining future cash flows at that reporting date.
2. That cash flows should reflect the perspective of the insurer.
3. How to distinguish between (a) cash flows that are incremental at the portfolio level, but need to be allocated to individual portfolios (for example, salaries of staff working on more than one portfolio) and (b) general overheads that do not relate to activities under the contracts. For this purpose, staff was asked to use existing cost guidance from other standards.

(IASB: 11 to 0, 4 absent; FASB: unaimous)

The Boards noted that, under the above principle, the following cash flows would be included in the measurement of the insurance contract:

1. The participating benefits an insurer expects to pay to policyholders of participating insurance contracts (that is, on an expected value basis). (IASB: 11 to 0, 4 absent; FASB: unanimous).
2. The incremental costs of selling, underwriting, and initiating an insurance contract, (acquisition costs), but only for those contracts that are actually issued. The Boards tentatively decided that an insurer should determine at the level of an individual contract whether those costs are incremental. (IASB: 8 to 3, 4 absent; FASB: unanimous)

Unbundling

The staff proposed an unbundling principle based on an assessment of whether there is significant interdependence between components of an insurance contract. However, the Boards questioned the clarity of the notion of significant interdependence.

Instead, the Boards asked the staff to develop an unbundling principle that uses as a starting point whether a component can introduce variability in the overall cash flows of the insurance contract for risks that are not considered part of the provision of insurance protection and, further, may consider factors such as:

1. The policyholder’s ability to obtain some or all of the contract value through withdrawal or redemption
2. The nature of the risks that are transferred by a component (for example, primarily financial or not).

The Boards tentatively decided that if development of an unbundling principle based on such a notion is not achievable, the forthcoming Exposure Draft will include an unbundling principle based on significant interdependence.

The Boards further decided that the forthcoming Exposure Draft should include guidance to help insurers understand when to unbundle a component of an insurance contract. That guidance will provide factors for consideration and examples. (IASB: 11 to 0, 4 absent; FASB: 5 unanimous)

Presentation

The Boards tentatively decided that an insurer should present income and expense for insurance contracts using a margin presentation, broadly showing the following items:

1. The change in the risk adjustment during the period [in the IASB's model that includes such an adjustment] and the release of the residual or composite margin during the period
2. The difference between the expected and the actual cash flows
3. Changes in estimates (remeasurements)
4. Interest on insurance liabilities (ideally presented or disclosed in a way that highlights its relationship with interest on assets backing those liabilities).

Consequently, an insurer should treat:

1. All premiums in the same way as deposits
2. All claims expenses, claims handling expenses, and other contract-related expenses in the same way as repayments of deposits.

This margin presentation (summarized margin presentation) will be supplemented by disclosures of those premiums and expenses.

The Boards acknowledged the importance of the presentation of the statement of comprehensive income, and the forthcoming Exposure Draft will ask respondents to provide specific input on this issue. (IASB: 11 to 0, 4 absent; FASB: unanimous)

Interest Accretion for Residual or Composite Margins

The Boards discussed whether interest should be accreted on residual and composite margins and, if so, which interest rate should be used.

The IASB affirmed its tentative decision to accrete interest on residual and composite margins and tentatively decided to use an interest rate that is locked in at inception of the contract. (IASB: 6 to 5, 4 absent)

The FASB affirmed its tentative decision not to accrete interest on residual and composite margins. (FASB: 3 to 2)

Next Steps

The IASB plans to publish an Exposure Draft in late July. The FASB plans to decide in July the best means for obtaining stakeholder input on the IASB proposal (for example, by publishing it as an Exposure Draft or in some other way).

General Announcements: None