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EXPOSURE DRAFT

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STAFF DRAFT
AUGUST 19, 2010
OF THE FINAL DRAFT ON

Financial Services—Insurance (Topic 944)

Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts

a consensus of the FASB Emerging Issues Task Force

SUBJECT TO CHANGE

An Amendment of the *FASB Accounting Standards Codification*™

Financial Accounting Standards Board
of the Financial Accounting Foundation

Notice to Recipients of This Staff Draft of an Accounting Standards Update on Financial Services—Insurance (Topic 944): Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts

This staff draft of an Accounting Standards Update has been prepared by the staff of the FASB for EITF Issue No. 09-G, "Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts." The draft reflects the cumulative, tentative conclusions made by the EITF culminating with its meeting on July 29, 2010. However, work on the Issue is continuing, and the proposals are subject to change before the EITF affirms as a final consensus and the Board decides to ratify that consensus and issue a final Accounting Standards Update.

The EITF decided to engage in additional outreach activities, such as soliciting fatal flaw comments from the Working Group, before affirming its consensus-for-exposure, which was previously published as an exposure draft of a proposed Accounting Standards Update on December 17, 2009.

After completing this outreach activity, the EITF will consider whether to change any of its tentative decisions in response to the input received. The EITF is not formally inviting comments on this staff draft; however, it welcomes input from interested parties. The EITF expects to reach a final consensus at its September 16, 2010 meeting.

More information about Issue 09-G is available on the FASB website www.fasb.org.

Accounting Standards Update

Financial Services—Insurance (Topic 944)

Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts

a consensus of the FASB Emerging Issues Task Force

August 2010

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Summary

Why Is the FASB Issuing This Accounting Standards Update (Update)?

The objective of this Update is to address diversity in practice regarding the interpretation of which costs relating to the acquisition of new or renewal insurance contracts qualify for deferral. The current definition of *acquisition costs* in the Master Glossary of the *FASB Accounting Standards Codification*™ is "costs that vary with and are primarily related to the acquisition of insurance contracts." Costs that meet that definition are typically recognized as assets and are commonly referred to as deferred acquisition costs.

Deferred acquisition costs are amortized over time using amortization methods dependent upon the nature of the underlying insurance product (that is, proportional to revenues, based on a contract's estimated gross profit, or based on a contract's estimated gross margin). Other costs that do not vary with and are not primarily related to the acquisition of new and renewal insurance contracts—such as those relating to investment management, general administration, and policy maintenance—are charged to expense as incurred.

As a result of the diversity in practice relating to the interpretation of which costs qualify as acquisition costs within the insurance industry, certain stakeholders initially raised the question of whether advertising costs meet the definition of acquisition costs. However, interpretation of the phrase, *vary with and are primarily related to* raises a broader conceptual issue that also applies to other types of costs; therefore, application of the amendments in this Update are not limited to advertising costs.

Who Is Affected by the Amendments in This Update?

The amendments in this Update affect insurance entities that are within the scope of Topic 944 (which includes but is not limited to stock life insurance entities, mutual life insurance entities, and property and liability insurance entities) that incur costs in the acquisition of new and renewal insurance contracts.

What Are the Main Provisions?

The amendments in this Update specify that the following costs incurred in the acquisition of new and renewal contracts should be capitalized in accordance with the amendments in this Update:

1. Incremental direct costs of contract acquisition incurred in transactions with independent third parties for that contract. Incremental direct costs are those costs that result directly from and are essential to the contract transaction and would not have been incurred by the insurance entity had that contract transaction not occurred.
2. Certain costs directly related to the following acquisition activities performed by the insurer for the contract:
   a. Underwriting
   b. Policy issuance and processing
   c. Medical and inspection
   d. Sales force 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 directly related to those activities that would not have been incurred if the contract had not been acquired.

Advertising costs should be included in deferred acquisition costs only if the capitalization criteria in the direct-response advertising guidance in Subtopic 340-20, Other Assets and Deferred Costs—Capitalized Advertising Costs, are met. If those criteria are met, the direct-response advertising costs should then be included as deferred acquisition costs for classification, subsequent measurement, and premium deficiency purposes in accordance with Topic 944. If the capitalization criteria in Subtopic 340-20 are not met, advertising costs are not included as deferred acquisition costs and should be accounted for in accordance with the guidance in Subtopic 720-35, Other Expenses—Advertising Costs.

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—should be charged to expense as incurred. Administrative costs, rent, depreciation, occupancy, equipment, and all other general overhead costs are considered indirect costs and should be charged to expense as incurred.

If the initial application of the amendments in this Update results in the capitalization of acquisition costs that had not previously been capitalized by an entity, the entity may elect not to capitalize those types of costs.

The amendments in this Update do not affect the guidance in paragraphs 944-30-25-4 through 25-5, which prohibits the capitalization of certain costs incurred in obtaining universal life-type contracts.

How Do the Main Provisions Differ from Current U.S. Generally Accepted Accounting Principles (GAAP) and Why Are They an Improvement?

The amendments in this Update modify the definition of the types of costs incurred by insurance entities that can be capitalized in the acquisition of new and renewal contracts. This revised definition may represent a significant change in practice for many insurance entities. For example, many insurance entities capitalize costs relating to unsuccessful contract acquisitions. The amendments in this Update specify that the costs must be based on successful efforts (that is, a new or renewal contract). The amendments also specify that advertising costs should only be included as deferred acquisition costs if the direct-response advertising criteria in Subtopic 340-20 are met.

The Board has an ongoing joint project on its agenda with the IASB on the accounting for insurance contracts. The Boards' current view in that project is that acquisition costs incurred for long-duration contracts should be included in the determination of the cash outflows of that insurance contract. The Board of the FASB has not concluded on the treatment of acquisition costs for short-duration contracts. The guidance from that joint project, if finalized, is not currently expected to be effective before 2014. By clarifying the acquisition costs that can be deferred now, the amendments in this Update improve current GAAP by providing a clearer definition of a qualifying capitalizable acquisition cost and, therefore, limits the significant diversity in practice that has developed in this area, particularly as it relates to the capitalization of costs related to unsuccessful acquisition efforts. This revised definition also improves consistency among insurance entities and financial institutions with respect to capitalizable costs because the definition is consistent with the types of costs that can be capitalized relating to loan originations in Topic 310, Receivables.

When Will the Amendments Be Effective?

The amendments in this Update are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2011. Early adoption is permitted. The amendments in this Update should be applied prospectively upon adoption. Retrospective application to all prior periods presented upon the date of adoption also is permitted, but not required.

How Do the Provisions Compare with International Financial Reporting Standards (IFRS)?

The guidance on deferred acquisition costs under IFRS is limited and is subject to significant judgment. IFRS neither prohibits nor requires the deferral of acquisition costs, nor does it prescribe which acquisition costs are deferrable, the period and method of their amortization, or whether an insurer should present deferred acquisition costs as an asset or as a reduction in insurance liabilities. IFRS 4, *Insurance Contracts,* is an interim standard and does not address the accounting for acquisition costs because in some cases those costs were an integral part of existing models and could not be amended easily without a more fundamental review of those models. While not necessarily applicable to insurance contracts, International Accounting Standard 39, *Financial Instruments: Recognition and Measurement,* limits capitalizable transaction costs for financial instruments to incremental costs that are directly attributable to the acquisition, issuance, or disposal of a financial asset or liability. IAS 39 defines an incremental cost as one that would not have been incurred if the entity had not acquired, issued, or disposed of the financial instrument.

Under the joint project on accounting for insurance contracts, the Boards have made preliminary conclusions on the accounting for acquisition costs. Those conclusions are tentative and could change upon further deliberation of the overall insurance models proposed by the Boards.

Amendments to the *FASB Accounting Standards Codification*™

Introduction

1. The Accounting Standards Codification is amended as described in paragraphs 2–13~~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 Master Glossary

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.~~ Costs that are ~~Acquisition costs include those costs that~~ ~~vary with and are primarily~~ directly related to the successful acquisition of new or renewal insurance contracts.

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 to obtain an insurance contract that has both of the following characteristics:

a. It results directly from and is essential to the acquisition of the contract.
b. It would not have been incurred by the insurance entity had that acquisition contract transaction not occurred.

Amendments to Subtopic 944-30

4. Supersede paragraph 944-30-25-1 and add paragraphs 944-30-25-1A through 25-1B, with a link to transition paragraph 944-10-65-1, as follows:

Financial Services—Insurance—Acquisition Costs

Recognition

944-30-25-1 Paragraph superseded by Accounting Standards Update No. 2010-XX. ~~**Acquisition costs** shall be capitalized. To associate such costs with related premium revenue, 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.~~ **[Content moved to paragraph 944-30-25-1B]**

944-30-25-1A Unless provided for in paragraph 944-10-65-1(d), an insurance entity shall capitalize only the following as acquisition costs:

a. **Incremental direct costs of contract acquisition** incurred in transactions with independent third parties for that contract (for implementation guidance, see paragraph 944-30-55-1).
b. The portion of the 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. Sales force contract selling.
c. Other costs directly related to the insurer's activities in (b) that would not have been incurred by the insurance entity had that acquisition contract transaction not occurred.
d. Advertising costs that meet the capitalization criteria in paragraph 340-20-25-4.

~~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:~~

944-30-25-1B ~~**Acquisition costs** shall be capitalized.~~ To associate {**add glossary link**} **acquisition costs** {**add glossary link**} 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. **[Content amended as shown and moved from paragraph 944-30-25-1]**

~~6~~.

5~~7~~. Amend 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.~~

6~~8~~. Amend paragraph 944-30-50-1, 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.

7~~9~~. Amend paragraph 944-30-55-1 and its related heading and add paragraphs 944-30-55-1A through 55-1M and their related headings, 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**:~~ Paragraph 944-30-25-1A(a) requires that an insurance entity capitalize **incremental direct costs of contract acquisition** incurred in transactions with independent third parties for that contract. Such costs include 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 for a successful contract acquisition.

>> Independent Third Parties

944-30-55-1A Independent third parties generally possess the following characteristics:

a. They are not employees of the insurer.
b. They are not receiving employee benefits of the insurer.
c. The party is not under the {**link to first definition**} **control** {**link to first definition**} of the insurer.

d. Generally, the party also would provide similar services to other entities unrelated to the insurer, and there would not be an agreement between the insurer and the party that precludes the party from providing similar services to other entities.

944-30-55-1B In determining whether an entity that provided contract acquisition-related services on behalf of the insurer could be considered an independent third party if the insurer has an ownership or equity interest in the entity, such ownership interest should be evaluated on the basis of the level of ownership and influence that could be imposed. Generally, the existence of an ownership interest indicates a relationship that would not qualify as an independent third party. A nominal passive investment from the standpoint of both the insurer and the provider of service probably would not affect the provider's independence.

944-30-55-1C If an entity utilizes a third party for contract acquisitions and the third party is not considered an independent third party for several reasons but also is not an employee of the entity, the entity should defer those costs directly related to specified activities that can be determined to meet the criteria in paragraph 944-30-25-1A(b) for acquisition costs under the definition of that term as long as those costs would not have been incurred by the insurance entity had that acquisition contract transaction not occurred.

>> Other Contract Acquisition Costs

944-30-55-1D Examples of other costs directly related to the insurer's activities in paragraph 944-30-25-1A(b) that would not have been incurred by the insurance entity had that acquisition contract transaction not occurred include all of the following:

a. Reimbursement of costs for air travel, hotel accommodations, automobile mileage, and similar costs incurred by personnel relating to the specified activities
b. Costs of itemized long-distance telephone calls related to contract underwriting
c. Reimbursement for mileage and tolls to personnel involved in on-site reviews of individuals before the contract is executed.

944-30-55-1E Paragraph 944-720-55-2 specifies that equipment costs (for example, an insurer's data processing equipment dedicated to acquiring insurance contracts), depreciation, and other general overhead must be charged to expense as incurred. Those costs do not meet the criteria for deferral as acquisition costs under the definition of that term because they would have been incurred whether or not a contract was acquired.

> > > Other Contract Acquisition-Related Costs

944-30-55-1F Costs for software dedicated to contract acquisition are not eligible for deferral as deferred acquisition costs under the definition of that term.

Such costs are not other costs related to those activities that would not have been incurred but for that contract under the definition of that term.

944-30-55-1G Payroll-related fringe benefits include any costs incurred for employees as part of the total compensation and benefits program. Examples of such benefits include all of the following:

a. Payroll taxes
b. Dental and medical insurance
c. Group life insurance
d. Retirement plans
e. 401(k) plans
f. Stock compensation plans, such as stock options and stock appreciation rights
g. Overtime meal allowances.

944-30-55-1H Bonuses based on successful acquisition or renewal of contracts that are paid to employees involved in contract acquisition activities are partially deferrable as acquisition costs under the definition of that term. Bonuses are part of an employee's total compensation. The portion of the employee's total compensation that may be deferred as acquisition costs is the portion that is directly related to time spent on the activities listed under the definition of that term and results in the origination of an insurance contract.

944-30-55-1I If compensation for an employee traditionally paid by salary or hourly wage is switched wholly or partially to commissions on successful contract acquisition or renewal, such costs would be partially deferrable as acquisition costs under the definition of that term. As specified in the preceding paragraph, only the portion of the employee's total compensation directly related to time spent on activities under the definition of that term for successful contracts would be deferred. Commission-based compensation arrangements between an insurer and its employees may be similar to arrangements an insurer may have with independent third parties, such as sales agents or brokers. However, when acquisition activities are performed by the insurer's employees, the insurer must allocate compensation costs applicable to the activities listed in the definition of acquisition costs on the basis of the portion of time spent by employees. An allocation of the employees' total compensation between contract acquisition and other activities is made so that only those costs associated with those acquisition activities listed under the definition of that term are deferred for successful contracts, even if commissions are 100 percent of such compensation and are based solely on successfully acquired contract transactions.

> > Cost Determination

944-30-55-1J This Subtopic does not specify how costs are to be determined but rather what costs must be deferred. In many instances, standard costing may be used to estimate the costs to be deferred in accordance with this Subtopic. For certain contracts, the cost of acquisition may be similar and standard costing may be appropriate for those contracts, while other contracts may be of such a nature that costs must be identified separately. Insurers may use any one or a combination of methods that will provide adequate information to report financial results in accordance with this Subtopic. Development of a standard costing system will require periodic analysis of variances and, if necessary, adjustment of standard costing estimates. Possible standard costing methods that may be used to measure costs applicable to transactions that have occurred, include standard costs, actual costs, job process costs (for example, homogeneous policies), or job order costs (for example, specific contracts).

944-30-55-1K The successful-efforts accounting notion utilized at an entity-wide level may result in a standard costing system that does not accurately reflect the amount of costs that may be deferred and amortized under this Subtopic. Successful acquisition efforts can be determined as a percentage of each function (for example, application, underwriting, and medical and inspection) and may be based on the percentage, adjusted for idle time and time spent on activities for which the related costs cannot be deferred, of successful and unsuccessful efforts determined for each function.

944-30-55-1L All other contract acquisition-related costs, including costs related to activities performed by the insurer for soliciting potential customers (except direct-response advertising capitalized in accordance with paragraph 944-30-25-1A(d)), market research, training, and administration, should be charged to expense as incurred. Employees' compensation and fringe benefits related to those activities, unsuccessful contract acquisition efforts, and idle time should be charged to expense as incurred. Administrative costs, rent, depreciation, and all other occupancy and equipment costs are considered indirect costs and should be charged to expense as incurred.

944-30-55-1M The portion of total compensation of executive employees that relates directly to the time spent approving successful contracts may be deferred as acquisition costs under the definition of that term. For example, the amount of compensation allocable to time spent by members of a contract approval committee is a component of acquisition costs.

Amendments to Subtopic 944-720

8~~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 Unless provided for in paragraph 944-10-65-1(d), ~~Paragraph 944-30-25-1~~ paragraph 944-30-25-1B ~~states that costs that are~~ requires that an insurance entity capitalize certain **acquisition costs** related to successful contracts~~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 that cannot be capitalized 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).

9~~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 and Illustrations

> 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 that cannot be capitalized in accordance with paragraph 944-30-25-1B. Such costs include costs of all of the following:

a. Soliciting potential customers (except direct-response advertising capitalized in accordance with paragraph 944-30-25-1A(d))
b. Market research
c. Training
d. Administration
e. Unsuccessful acquisition or renewal efforts (except direct-response advertising capitalized in accordance with paragraph 944-30-25-1A(d))
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 all of the following:

a. Administrative costs
b. Rent

c. Depreciation
d. Occupancy costs
e. Equipment costs
f. Other general overhead.

10~~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 in either of the following ways:
   1. On a prospective basis in fiscal years beginning after December 15, 2011, and interim periods within those fiscal years. If an entity applies the pending content that links to this paragraph prospectively, an entity shall disclose either of the following instead of the disclosure required by paragraph 250-10-50-1(b)(2) in the period of adoption:
      i. The amount of **acquisition costs** that would have been capitalized during the corresponding period immediately preceding adoption as if the guidance in the pending content that links to this paragraph had been applied during that period compared with the amount previously capitalized during that period.
      ii. The amount of acquisition costs capitalized during the period of adoption compared with 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.
   2. On a retrospective basis to all prior periods as described in paragraphs 250-10-45-6 through 45-7. If an entity applies the pending content that links to this paragraph retrospectively, an entity is not required to make the disclosure required by paragraph 250-10-50-1(b)(2) for the period of adoption.

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 except as noted above for paragraph 250-10-50-1(b)(2).
d. If the application of the pending content would result in the capitalization of **acquisition costs** that had not previously been

capitalized by the entity before adoption of the pending content, the entity may elect not to capitalize those types of costs.

11. Amend paragraph 944-30-00-1 as follows:

944-30-00-1 The following table identifies the changes made to this Subtopic. ~~No updates have been made to this subtopic.~~

Paragraph Number	Action	Accounting Standards Update	Date
Acquisition Costs	Amended	2010-XX	08/XX/2010
Incremental Direct Cost of Contract Acquisition	Added	2010-XX	08/XX/2010
944-30-25-1	Superseded	2010-XX	08/XX/2010
944-30-25-1A	Added	2010-XX	08/XX/2010
944-30-25-1B	Added	2010-XX	08/XX/2010
944-30-25-2	Amended	2010-XX	08/XX/2010
944-30-50-1	Amended	2010-XX	08/XX/2010
944-30-55-1	Amended	2010-XX	08/XX/2010
944-30-55-1A through 55-1M	Added	2010-XX	08/XX/2010

12. Add paragraph 944-720-00-1 as follows:

944-720-00-1 The following table identifies the changes made to this Subtopic.

Paragraph Number	Action	Accounting Standards Update	Date
Acquisition Costs	Amended	2010-XX	08/XX/2010
944-720-25-1	Amended	2010-XX	08/XX/2010
944-720-25-2	Amended	2010-XX	08/XX/2010
944-720-55-1	Added	2010-XX	08/XX/2010
944-720-55-2	Added	2010-XX	08/XX/2010

13. Amend paragraph 944-10-00-1 as follows:

944-10-00-1 The following table identifies the changes made to this Subtopic. ~~No updates have been made to this subtopic.~~

Paragraph Number	Action	Accounting Standards Update	Date
Acquisition Costs	Amended	2010-XX	08/XX/2010
944-10-65-1	Added	2010-XX	08/XX/2010

Add Board vote when ready.

Background Information and Basis for Conclusions

Introduction

BC1. The following summarizes the Task Force's considerations in reaching the conclusions in this Update. It includes the Board's basis for ratifying the Task Force conclusions when needed to supplement the Task Force's considerations. It also includes reasons for accepting certain approaches and rejecting others. Individual Task Force and Board members gave greater weight to some factors than to others.

Background Information and Conclusions

BC2. As a result of the diversity in practice relating to the interpretation of which costs qualify as acquisition costs within the insurance industry, certain stakeholders initially raised the question of whether advertising costs meet the definition of acquisition costs. However, interpretation of the phrase *vary with and are primarily related to* in the definition of acquisition costs raised broader conceptual issues that also applied to other types of costs; therefore, the Task Force decided that the resolution of this Issue should not be limited to advertising costs.

BC3. At the November 19, 2009 EITF meeting, the Task Force reached a consensus-for-exposure on EITF Issue No. 09-G, "Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts." A proposed Accounting Standards Update (proposed Update) was issued on December 17, 2009, with a comment period that ended on February 12, 2010. Twenty comment letters were received on the proposed Update. Additionally, a Working Group was formed to assist the staff in advising the Task Force on the effective date and transition questions. 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. Several Task Force members also observed and participated in the meeting. The Working Group met on May 13, 2010.

BC4. In discussing this Issue, some Task Force members indicated that, in their view, only costs that are both direct and incremental and are incurred as a result of obtaining new or renewal contracts should be considered acquisition costs, while other members preferred expensing all contract acquisition costs. Other

Task Force members favored aligning the nature of capitalizable costs in contract acquisition activities with those capitalizable costs of loan origination activities in Topic 310. That model encompasses both direct and incremental costs and certain additional direct costs incurred to complete successful contract acquisitions or renewals.

BC5. Some Task Force members noted that the loan origination model does not permit capitalization of costs relating to unsuccessful loan efforts, which, if applied by insurance companies, would result in a significant change from current practice. Other Task Force members questioned the conceptual basis for how costs relating to unsuccessful contract acquisition efforts could be considered to provide a future economic benefit to warrant asset recognition.

BC6. The Task Force concluded 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 and that costs related to unsuccessful contract efforts should be expensed as incurred. The Task Force also decided that incremental direct costs of contract acquisition incurred in transactions with independent third parties and that certain additional direct costs incurred by the insurer to complete successful contract acquisitions or renewals should be capitalized.

BC7. During the deliberations of this Issue, the Task Force discussed 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. The Task Force affirmed its consensus-for-exposure that advertising costs should be capitalized only if the criteria for capitalizing such costs in accordance with the direct-response advertising guidance in Topic 340 were met. The Task Force concluded that after those criteria are met, the direct-response advertising costs should be included as deferred acquisition costs for classification, subsequent measurement, and premium deficiency purposes in accordance with Topic 944.

Effective Date and Transition

BC8. The Task Force decided that the amendments in this Update should be effective for fiscal years beginning on or after December 15, 2011. The Task Force decided that early application of the amendments should be permitted.

BC9. As a result of the feedback provided by the Working Group, the Task Force supported a deferral of the effective date of the originally proposed Update. The Task Force 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 deferred acquisition cost internal controls.

BC10. The Task Force concluded that if, as a result of applying the guidance in this Update, entities are required to capitalize more costs than are being capitalized currently, those entities should not be required to capitalize the additional costs. The Task Force did not believe it would be beneficial for insurers to incur costs to develop new systems to capitalize additional acquisition costs, particularly if they may have to expense all acquisition costs as part of the Board's project on insurance contracts.

BC11. The Task Force decided to require prospective application upon the date of adoption and concluded that retrospective application is also permitted, but not required. The Task Force also decided to require certain transition disclosures. The Task Force concluded that if an entity chooses to apply the guidance in this Update prospectively, the entity would be required to disclose one of the following disclosures instead of the disclosures required by paragraph 250-10-50-1(b)(2) in the period of adoption:

a. The amount of acquisition costs that would have been capitalized during the corresponding period immediately preceding adoption as if the guidance in the pending content that links to this paragraph had been applied during that period compared with the amount previously capitalized during that period.
b. The amount of acquisition costs capitalized during the period of adoption compared with 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.

BC12. The Task Force also concluded that if an entity chooses to apply the guidance retrospectively, the entity would not be required to disclose the effect of the change in the current period as required by paragraph 250-10-50-1(b)(2). However, the other disclosures required by paragraphs 250-10-50-1 through 250-10-50-3 would be required under both prospective and retrospective application.

Benefits and Costs

BC13. The objective of financial reporting is to provide information that is useful to present and potential investors, creditors, donors, and other capital market participants in making rational investment, credit, and similar resource allocation decisions. However, the benefits of providing information for that purpose should justify the related costs. Present and potential investors, creditors, donors, and other users of financial information benefit from improvements in financial reporting, while the costs to implement new guidance are borne primarily by present investors. The Task Force's assessment of the costs and benefits of issuing new guidance is unavoidably more qualitative than quantitative because there is no method to objectively measure the costs to implement new guidance or to quantify the value of improved information in financial statements.

BC14. The Task Force anticipates that entities will incur incremental costs to implement the amendments in this Update. The most significant incremental costs are expected to be associated with allocating costs between successful efforts and unsuccessful efforts if entities had not previously performed such an analysis or do not currently capture information in that manner. However, the Task Force believes that the improvements to financial reporting, such as a reduction in the diversity in practice in the types of costs capitalized and the elimination of costs that have been capitalized relating to unsuccessful efforts, are in excess of costs to implement the new guidance. In deliberating this Issue, the Task Force also considered the tentative conclusions reached by the Boards as part of their joint project on insurance contracts. Specifically, the Task Force considered that the guidance from that project, once finalized, is not currently expected to be effective before 2014. As such, the Task Force believes that by clarifying the acquisition costs that can be deferred now, the amendments in this Update improve current GAAP by providing a clearer definition of a qualifying capitalizable acquisition cost and, therefore, limit the significant diversity in practice that has developed in this area, particularly as it relates to the capitalization of costs related to unsuccessful acquisition efforts, and that those benefits justify the costs of implementing the requirements of the Update.

Amendments to the XBRL Taxonomy

The following elements or modifications to existing elements are proposed additions to the XBRL U.S. GAAP Financial Reporting Taxonomy. They reflect the amendments to the disclosure and presentation requirements of the Accounting Standards Codification and would be used in association (tagged) with the appropriate reported values in the SEC filer XBRL database. (Elements that currently exist in the 2009 taxonomy are marked with an asterisk* and have been **bolded.** If an existing element was modified, it has been marked to reflect any changes.)

Standard Label†	Definition	Codification Reference
Type of Deferred Policy Acquisition Costs	Describes the type of costs that are included as deferred policy acquisition costs. Acquisition costs are directly related to the successful acquisition of new and renewal insurance contracts.	944-30-50-1(a) 944-30-55-1
Deferred Policy Acquisition Costs Disclosure*	Describes the nature<u>, type</u>, and amount of capitalized costs incurred to write or acquire insurance contracts, the basis for and methodology for capitalizing such costs, the accounting for such deferred acquisition costs (DAC) when modifications or internal replacements of related insurance contracts occur and the effect on results of operations, and the methodology and amount of amortization.	944-30-50-1 944-210-S99-1 944-30-50-4
Deferred Policy Acquisition Costs Net*	The unamortized portion as of the balance sheet date of capitalized <u>policy acquisition </u>costs~~ that vary with and are primarily related to~~	944-210-S99-1 944-30-45-1 944-30-55-1

†The Standard Label and the Element Name are the same (except that the Element Name does not include spaces). If they are different, the Element Name is shown in *italics* after the Standard Label.

Standard Label[†]	Definition	Codification Reference
	~~the acquisition of new and renewal insurance contracts and coverages~~.	
Nature of Deferred Policy Acquisition Costs*	Describes the nature of costs incurred in the successful acquisition of new and renewal insurance contracts~~, including those costs that vary with and are primarily related to the acquisition of new contracts (for example, agent and broker commissions, certain underwriting and policy issue costs, and medical and inspection fees)~~.	944-210-S99-1 944-30-55-1 944-30-50-1(a)
Capitalization of Deferred Policy Acquisition Costs, Policy*	Describes an insurance entity's accounting policy for deferred policy acquisition costs, including the nature, type, and amount of capitalized costs incurred to write or acquire insurance contracts, and the basis for and methodologies applied in capitalizing and amortizing such costs.	235-10-50-3 944-30-50-1
Deferred Policy Acquisition Costs [Text Block]*	This element may be used as a single block of text to encapsulate the entire disclosure, including data and tables, pertaining to the nature, type, and amount of capitalized costs incurred to write or acquire insurance contracts, the basis for and methodology for capitalizing such costs, the accounting for such deferred acquisition costs (DAC) when modifications or internal replacements of related insurance contracts occur, the effect on results of operations,	944-30-50-1 944-210-S99-1 944-30-50-4

Standard Label[†]	Definition	Codification Reference
	and the methodology and amount of amortization.	
Deferred Policy Acquisition Costs and Present Value of Future Profits, Disclosure*	Describes the nature, type, and amount of costs ~~incurred in~~that relate to the successful acquisition of new and renewal insurance contracts~~, including those costs that vary with and are primarily related to the acquisition of new contracts (for example, agent and broker commissions, certain underwriting and policy issue costs, and medical and inspection fees),~~ and in connection with the purchase of a life insurance company, describes the nature and amounts of the present value of future profits (PVFP) of estimated net cash flows embedded in the existing long-duration contracts of the acquired entity, reconciles the carrying value from the beginning to the end of the period, and provides other information pertinent to an understanding of PVFP, which is also known as value of business acquired, or VOBA.	944-30-50-1(a) 944-20-S99-2
Deferred Policy Acquisition Costs and Present Value of Future Profits, Additions*	Additions during the period in (a) capitalized policy acquisition costs~~ that vary with and are primarily related to the acquisition of new and renewal insurance contracts and coverages~~, and (b) capitalized present value of future profits (also known as value of business acquired).	944-20-S99-2(2)
Supplemental	Amount of deferred policy	944-235-S99-3

Standard Label†	Definition	Codification Reference
Information for Property, Casualty Insurance Underwriters, Deferred Policy Acquisition Costs*	acquisition cost related to property-casualty insurance policy written.~~ Policy acquisition costs are costs that vary with and are primarily related to the acquisition and renewal of insurance contracts during the period (for example, commissions, salaries of underwriting personnel, inspection fees).~~	
Deferred Policy Acquisition Costs and Present Value of Future Profits*	The sum of the unamortized portion as of the balance sheet date of (a) capitalized policy acquisition costs~~ that vary with and are primarily related to the acquisition of new and renewal insurance contracts and coverages~~, and (b) capitalized present value of the future profits (also known as value of business acquired).	944-20-S99-2(2) 944-210-S99-1 944-30-50-1(a)
Supplemental Information for Property, Casualty Insurance Underwriters, Amortization of Deferred Policy Acquisition Costs*	Amount of amortization expense on deferred policy acquisition costs.~~ Deferred policy acquisition costs are costs that vary with and are primarily related to the acquisition or renewal of insurance contracts during the period (for example, commissions, salaries of underwriting personnel, inspection fees).~~	944-235-S99-3