



On Your Side®

October 25, 2013

Technical Director
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, Connecticut 06856-5116

Re: File Reference No. 2013-290 - Proposed Accounting Standards Update, *Insurance Contracts (Topic 834)*

Dear Technical Director:

We appreciate the opportunity to comment on the exposure draft of the Proposed Accounting Standards Update, *Insurance Contracts (Topic 834)* (“the Proposed ASU”). Nationwide and Subsidiaries (“Nationwide”) is comprised of three affiliated mutual insurance companies and their subsidiaries under common management, operating both property and casualty and life insurance companies. Nationwide is a Fortune 100 company and one of the largest diversified insurance and financial services organizations in the world, with assets totaling \$170 billion.

While we have supported and continue to support the efforts of the Financial Accounting Standard Board (“the FASB” or “the Board”), and its work with the International Accounting Standards Board (“the IASB”) toward the broader objective of achieving a converged international standard of accounting for insurance contracts, we do not believe that the Proposed ASU achieves the key objectives of the FASB or represents an overall improvement to current U.S. GAAP for the accounting of insurance contracts. Specifically, we do not believe the improvements in the Proposed ASU outweigh the costs and complexities of implementation. Rather, current U.S. GAAP should be evaluated separately by the Board to facilitate tailored improvements to the insurance contracts accounting models. Further, we believe implementing the Proposed ASU would negatively impact the comparability, relevance, understandability and decision-usefulness of our financial statements, which would result in the increased usage of non-GAAP measures to analyze an insurance company.

Despite the efforts of the Board and the IASB to work on the insurance contracts project jointly, many key aspects of the proposed guidance are not converged. This non-convergence will create significantly different results between U.S. and international companies, undermining the comparability that would result from the application of the Proposed ASU. Furthermore, there are aspects of the Proposed ASU which either involve a significant amount of complexity or uncertainty in interpreting the guidance, which we believe would further result in the Board not meeting its objective to provide more comparable financial statements.

In order to be meaningful and decision-useful to management and financial statement users, we believe the accounting for insurance contracts should reflect how the business is managed and how risk management practices are utilized. As drafted, the Proposed ASU overlooks the core fundamentals of the insurance business, and in doing so provides misleading information. Although the Board has provided the ability to reflect discount rate changes through other comprehensive income (“OCI”), we believe that due to the discount rate methodology

within the Proposed ASU, significant accounting mismatches will continue to result between the insurance contract liabilities and the related financial assets. This will inherently drive significant financial statement volatility for insurers, which may not be indicative of an entity's overall financial performance. As we believe this proposed accounting model does not fairly represent the economics of the insurance business, we are concerned that insurers may change behavior to manage financial statement accounting volatility, resulting in additional costs to be borne by policyholders. For example, management may choose to purchase new hedging instruments simply to dampen accounting volatility created by the Proposed ASU. Alternatively, management may reduce the availability or change the pricing of certain products, such as spread-based life and annuity products, to achieve a more accurate pattern of future accounting earnings that does not reflect day-one accounting losses. We prefer an accounting model that is more reflective of our business economics, so that downstream pricing and product availability impacts are minimized.

Overall, the Proposed ASU will increase the complexity of accounting for insurance contracts, which will result in even less consistency and comparability between companies, hindering a financial statement user's ability to make critical decisions based on a company's performance and financial condition. A core principle in the creation of the Proposed ASU is to provide relevant information for financial statement users; however, analysts and other financial statement users have indicated that the Proposed ASU will create a method of reporting that is not easily understood or decision-useful. This will likely necessitate significant efforts to develop even more pervasive non-GAAP metrics than are currently used today.

We understand the Board may be focused more on the "potential" investors of the insurance industry, who may shy away from insurance companies because insurance accounting is viewed as a "black box"; however, we do not believe the application of the Proposed ASU would make the insurance contract model any more transparent to investors. Although we can appreciate the Board's efforts to expand the pool of potential investors, we believe these investors have not ventured into the industry mostly due to the inherent complexities of the insurance business model. These complexities will not change regardless of whether new accounting standards are developed and we believe that the Proposed ASU will only increase the difficulty of understanding the business. If the Board proceeds with the Proposed ASU, not only will "potential" investors lack insights into the economics or management of the insurance business based on the financial statements, but the current financial statement users will also be negatively impacted. In fact, an overwhelming majority of preparers and current users, who have a firm understanding of the true economics underlying the insurance business model, do not find this proposed model to be reflective of the business. Instead of improving investors' and analysts' comprehension of insurance companies and thereby potentially bringing new investors into the insurance industry, we believe the added complexity and misalignment with the underlying economics will have the unintended effect of driving investors away, resulting in increased cost of capital for insurers and ultimately impacting the pricing insurers can provide their customers. We believe that it is imperative for the Board to utilize the feedback received from investors, analysts and financial statement users in assessing whether the Proposed ASU provides decision-useful information that represents an improvement to current U.S. GAAP.

Lastly, the insurers will incur significant costs to adopt the Proposed ASU, the benefits of which are unclear given that the stated objectives have not been met. We encourage the Board to consider the significant economic impact to the preparers of the financial statements to implement these comprehensive changes, as well as the resulting downstream impacts to policyholders, investors, analysts and other financial statement users. We believe that the Board could provide a greater benefit to financial statement users at a lower cost if targeted improvements to current U.S. GAAP were pursued, versus the Proposed ASU's full replacement of the accounting for insurance contracts. While this response does not identify areas where we believe targeted improvements to existing U.S. GAAP may be warranted, we acknowledge that the Board has identified a number of areas within the Proposed ASU where targeted improvements to existing U.S. GAAP may be justified. We would appreciate the opportunity to discuss those areas and potentially others with the Board further, if the Board decides to take our recommendation to pursue this approach instead of the Proposed ASU.

If the Board, nonetheless decides to proceed with the Proposed ASU, we respectfully request it considers the following key recommendations and concerns relating to the Proposed ASU.

➤ Measurement

- The definition of a portfolio should be modified to group insurance contracts that are “managed together as a single pool”. Indicators that a set of contracts qualifies as a portfolio may include that the contracts are subject to similar risks, expected to have similar patterns of release from risk, priced similarly relative to the risk assumed, or priced together.
- Clarification is needed on the guidance to determine fulfillment cash flows, to ensure that proven actuarial methods currently used today, as well as concepts such as the “actuarial central estimate” utilized within the property and casualty insurance industry, satisfy the intent of the proposal.
- Discounting the liabilities for remaining coverage and the incurred claims associated with contracts to be accounted for using the Premium Allocation Approach (“PAA”), without adequately reflecting the risk inherent in those cash flows, creates an unbalanced financial statement presentation that is less meaningful than current U.S. GAAP. In addition, to implement the discounting requirement, significant costs will be incurred by an insurer, for which the benefits are unjustified.
- If it can be demonstrated that certain liabilities and assets are managed together as part of a risk management strategy, the associated discount rate used in the measurement of the liability should be linked to the rate used to price the insurance contract, to promote consistent financial results for the asset and liability.
- Recording an expected loss for a potential catastrophic event as a result of the onerous contracts provision within the Proposed ASU does not provide a faithful representation of an insurer’s liability. Consistent with current U.S. GAAP, liabilities for catastrophic events should not be recognized until an event has occurred, the event adversely affects the policyholder and the loss can be reasonably estimated.
- The recognition of expected losses should be based upon the actual economic nature of an insurance contract, and include all critical revenue streams that are considered when managing the profitability of an insurance contract. Exclusion of critical revenue streams from the Building Block Approach (“BBA”) and onerous contract tests under both approaches will result in loss recognition that is not reflective of the economics of the business and will mislead financial statement users.
- The margin should be unlocked to allow adjustment of the margin as if the changes in estimated cash flows were known at the inception of the insurance contract. Unlocking the margin to reflect changes in future estimated cash flows would provide a more faithful representation of the expected profitability of an insurance contract and better portray the results of the business.

➤ Financial Statement Presentation

- The Board should reevaluate the overall financial statement presentation approach to determine an alternative approach that not only meets the Proposed ASU’s objective of providing relevant and useful information that faithfully represents the nature and economics of an entity’s insurance contracts, but also has support of investors, analysts, management and other financial statement users.
- The revenue recognition approach in the Proposed ASU will not provide decision-useful information to financial statement users from companies that issue life insurance and other long-term insurance contracts.
- Investment income earned on segregated fund arrangements should be offset by subsequent pass-through of the investment earnings and not presented on the statement of comprehensive income, consistent with current U.S. GAAP.

➤ Transition

- As the Proposed ASU represents significant and fundamental changes to the accounting for insurance contracts, we believe that the effective date should be no earlier than six years after the issuance of the final standard.
- Entities with both public and nonpublic entities in their organizational structure should have the option to adopt the Proposed ASU for the nonpublic entities concurrently with the effective date for the public entities, allowing for consistency of application, stream-lined reporting and efficient implementation activities.
- As the Proposed ASU requires retrospective application, we believe preparers should be allowed to use hindsight to reflect known developments in the industry and/or economy, such as economic downturns and recoveries, in the estimates as they apply the provisions of the Proposed ASU to prior periods.

We expound on our key recommendations and concerns in the following pages.

COMPREHENSIVE RECOMMENDATIONS AND CONCERNS:

Measurement

Unit of Account

We believe that the definition of a portfolio should center on how the business is managed, since that factor most significantly affects how a company is differentiated and derives value and as such should underlie the measurement of a company's insurance contracts to create decision-useful information. Current U.S. GAAP requires an insurance company to group its contracts consistent with its manner of acquiring, servicing and measuring the profitability of its insurance contracts. This requirement acknowledges the linkage between the definition of a portfolio and how the insurance contracts are being managed as a group. Although we believe this definition has stood the test of time, we acknowledge that the Board wants to update it. As such, we believe the definition of a portfolio should be modified to group insurance contracts that are "managed together as a single pool." Indicators that the insurance contracts are managed together as a single pool may include that they are subject to similar risks, expected to have similar patterns of release from risk, priced similarly relative to the risk assumed, or priced together.

As proposed, the definition of portfolio is not aligned with the manner in which insurance companies manage their business, which will significantly increase the cost of implementing and the complexity of applying this standard. We believe this added complexity will ultimately result in differences in application among companies. We have concerns with this definition due to the unintended consequences it has on all aspects of the model (e.g., onerous contracts, margin and discount rate determination, etc.). We believe that if the criterion is left as currently proposed, the result will be insurance companies tracking a voluminous number of portfolios.

While we are concerned with the overall proposed definition of portfolio, we have significant concerns regarding the duration requirement in particular and the impact on contracts with multiple perils. The duration requirement seems to suggest that an entity could not combine life insurance policies issued to thirty-year olds and fifty-year olds that are exactly the same, because different age groups may have different expected durations. Further, it would seem the duration requirement would force companies to bifurcate multiple peril insurance contracts (e.g., physical damage versus liability, etc.) due to different durations for these perils. As the definition refers only to groupings of contracts, not portions of contracts, we believe the intention is not to require bifurcation at this level into separate portfolios.

The permutations of these proposed criteria (subject to similar risks, priced similarly relative to the risks assumed, similar duration, and similar patterns of release from risk) will force companies to an undue level of granularity, which will exacerbate the costs of applying this standard and lead to less meaningful results. For example, a focus on pricing with no consideration of the diversification strategies management has put in place ignores a core fundamental of the insurance business model. We believe modifying the proposed portfolio definition as discussed above will allow companies to measure their contracts in a manner which more faithfully represents how the business is managed, providing financial statement users with reliable and relevant financial information while reducing the costs of applying the Proposed ASU.

Unbiased Probability Weighted Cash Flows

To satisfy the intent of the proposed measurement model, we propose further guidance and clarification to specifically support current actuarial methods and concepts, such as the “actuarial central estimate” utilized today within the property and casualty insurance industry. We share the significant concern of the actuarial community with the verbiage “unbiased probability weighted estimate” included in the Proposed ASU and with the practical implications of how that may be applied to insurance contracts under the PAA. It could be interpreted that the ability of an actuary to weigh the scenarios in the methodology used would indicate that an estimate can never be truly “unbiased.” In addition, some in the industry believe that to comply with this requirement, a purely statistical method would need to be established; however, such an approach would be overly restrictive and inconsistent with best practice.

We believe that the best description of property and casualty cash flow estimates may be derived from the current guidance promulgated by the American Academy of Actuaries’ Actuarial Standards Board, in their publication titled *Actuarial Standard of Practice No. 43, Property/Casualty Unpaid Claim Estimates* (“ASOP 43”). This publication describes the actuarial central estimate as “an estimate that represents an expected value over the range of reasonably possible outcomes.” ASOP 43 provides further clarification that “an actuarial central estimate may or may not be the result of the use of a probability distribution or a statistical analysis. This description is intended to clarify the concept rather than assign a precise statistical measure, as commonly used actuarial methods typically do not result in a statistical mean.”

We believe it is not the Board’s intention to comprehensively change current and historically proven actuarial methods, but rather to remove unsupported management estimates and ensure that liabilities are measured based on established actuarial principles. Likewise, we believe the Board seeks to require appropriate rationalization and support for any management adjustments to these actuarially determined values. We request that the Board clarify the intention of the guidance, to (1) specifically support actuarial methods and actuarial standards of practice currently in use today within the property and casualty industry, and (2) allow management adjustments to the actuarially determined expected values with appropriate rationalization and support, based upon management’s expertise and thorough understanding of the business. We do not believe it appropriate to require that a statistical modeling approach be used to derive loss reserve estimates, as that approach has not been proven to be sufficiently reliable or accurate and would potentially preclude the incorporation of vital qualitative information from the reserving process, resulting in diminished accuracy. It also would result in a fundamental change in how the claims reserving process is understood by analysts and other financial statement users, would limit the use of historically proven actuarial methods, and would result in a significant change in claims reserving practices for the property and casualty insurance industry.

For life and other long-term insurance contracts that apply the BBA, if it is the Board’s intention to allow only a stochastic modeling approach to derive a purely statistical mean for determining fulfillment cash flows, this will consequently provide less decision-useful information and affect the comparability of insurance contract liabilities between companies, due to the increased usage of standard scenario generators that will not be dictated. To meet the Proposed ASU’s key objectives of increasing comparability and providing decision-

useful information, we support the use of deterministic models, when appropriate, which will provide increased comparability and transparency in the liability measurement for insurance contracts.

Discounting –PAA

While we understand the theoretical merit of considering the time value of money as it relates to the fulfillment of insurance contract liabilities, we do not agree that an entity should discount the reserves (i.e., the liability for remaining coverage and liability for incurred claims) calculated under the PAA model. Discounting requires the estimation of both the amount and timing of cash flows. In the property and casualty business, where most contracts would follow the proposed PAA model, the timing of the cash flows is uncertain, unlike a life insurance contract where the benefits are able to be modeled. Discounting reflects the time value of money, but ignores the risk of uncertainty in the cash flows and additionally introduces new interest rate risk to the balance sheet. Discounting these reserves may also give financial statement users a false sense of confidence in an insurer's ability to estimate the timing of these reserves. This creates comparability issues between companies and will provide less decision-useful information to the financial statement users. Further, the current standard of not discounting the reserves provides an implicit risk margin for the reserves. We believe this is prudent given the complexities in the estimation process, as well as the inherent unknowns associated with the timing of payments. Though an imprecise risk margin, this standard is well established in both U.S. GAAP and statutory accounting and consequently understood by analysts, existing and potential investors, regulators and other financial statement users.

Furthermore, as we do not support discounting for contracts measured under the PAA, we are not promoting the combination of discounting and the use of a separate explicit risk margin. Such an approach would add significant cost and uncertainty and not be viewed as an improvement over current practice. An explicit risk margin would not be able to be reliably calculated and its use would make published financial results less transparent and comparable.

Finally, based on discussions with analysts and other financial statement users, users will not use the discounted amounts; rather, they will adjust those amounts back to the undiscounted liability amounts. We understand that the Board believes that the analysts and users will become accustomed to the financial statements in the manner required under the Proposed ASU. However, we believe that this perception is not focused on what the user community wants. We believe that discounting has resulted in a failed attempt at transparency in the past (e.g., pension accounting), and we do not want to see that happen for reserves associated with the PAA. The liability for remaining coverage and the liability for incurred claims should be measured in a manner that is useful to the financial statement users. It's true that discounting the liabilities would provide financial benefit to companies utilizing the PAA through bolstering capital and reducing liabilities, but the industry believes so strongly that discounting under the PAA will not provide more relevant information to the financial statement users that the industry is looking beyond this benefit, to reflect what we believe to be a more appropriate representation of our liabilities to policyholders.

We believe retaining this requirement will result in significant implementation costs and financial statements that are less comparable, decision-useful and relevant than financial statements under existing accounting standards..

We do not support the discounting requirement for contracts accounted for using the PAA, as we believe reflecting discounting as proposed would result in a less than faithful representation of our liabilities. As an alternate approach, though, if done at an appropriate level, we would support providing a sensitivity analysis for contracts accounted for using the PAA. As stated above, we agree with the theoretical merit of considering the time value of money, but due to the nature of the liabilities to be accounted for using the PAA, we believe this consideration would be more meaningful and relevant when provided as a range of possible discount rate impacts. Additionally, this alternative would significantly reduce the costs of applying this standard.

Finally, if the Board moves forward with discounting, we believe that the Board should allow the use of a risk-free rate alone to discount these reserves. Although the risk-free rate will not contain all of the characteristics inherent in the reserves, it will be the most significant component of the discount rate, especially as it pertains to contracts accounted for under the PAA, which would generally be thought to have less illiquidity than those contracts accounted for under the BBA. As the discount rate will be less than the method prescribed under the Proposed ASU, it will inherently incorporate a risk adjustment in the amount and will result in higher reserves. Further, as the development of the liquidity premium added to the risk-free rate involves more judgment, eliminating the liquidity adjustment from the discount rate development would promote consistency and comparability among companies required to discount using the PAA.

Method to Calculate the Discount Rate

We agree that the approach for calculating the discount rates should not be prescribed by the Proposed ASU, but rather determined using a principles-based approach. Depending on the company and its asset and liability management processes, a principles-based approach would provide companies with the flexibility to apply the guidance consistently with how they manage their business. A significant portion of insurance business consists of long-term liabilities that are priced and managed in concert with the assets backing them, in order to provide for the ultimate cash flows along with a provision for profit. As such, we believe the interest rate, explicit or implicit, used in the pricing of an insurance contract would generally be the appropriate discount rate, as this rate reflects the characteristics of the insurance contract liability that can be observed at the time of issuance. When an asset liability management strategy is being adhered to, this rate would be similar or identical to the expected earned rate on the assets backing the contract, net of expected default losses. The pricing rate is reflected directly in the premiums charged to the customer and is a rate that would prevent losses (or a significantly reduced margin) at inception for portfolios of contracts that are expected to be profitable overall. Therefore, it reflects the most likely outcome of the insurance activity as a whole, considering the underwriting and investment function together.

We understand the Board may be concerned about using a pricing rate in the current fulfillment model, as rates may have significant movements in the days following the sale of the insurance contract. However, we believe that such movements could be taken into consideration through an update, to reflect the interest rate used in pricing new insurance contracts with similar features. In the absence of unusual pricing or investment activity, the updated pricing rate is likely to continue to be the future expected earned rate, but be measured as of that new point in time. To the extent interest rates have moved in the interim, the asset fair values would have moved accordingly, and the expected earned rate from those assets would have changed appropriately to reflect the changed economic environment.

We recognize that there may be unusual situations that would not support the presumption that the pricing rate (i.e., the expected earned rate adjusted for defaults) represents a rate that reflects the characteristics of the liability. Examples of when using a pricing rate would be inappropriate would be an entity under-pricing the market to gain market share or over-pricing the market to effectively leave a market. Indicators could be provided by the Board for insurers to use to assess if their own expected asset earned rate is not consistent with the characteristics of the insurance contract liability. One indicator may be if the entity's prices are out of line with competitors' prices for similar products, or if its prices are out of line with reinsurance prices for ceding similar risks. However, in the absence of evidence to the contrary, the rebuttable presumption should be that the insurer's own expected earned rate, net of expected defaults, reflects the rate consistent with the characteristics of the insurance contract liability.

By not considering the rate used to price the insurance contract, a complete picture of the company's financial results cannot be seen, which results in less relevant financial information. Ultimately, disregarding the critical inter-relationship between assets backing insurance liabilities in determining the discount rate to be

used in the measurement of those liabilities would be to the detriment of the financial statement users and would make U.S. GAAP reporting significantly less meaningful to management.

Consideration of Catastrophic Events in an Onerous Contracts Test

We do not agree with the inclusion of potential catastrophic events in an onerous contract test, as portrayed in Example 13 of the Board's Proposed ASU. The uncertain nature of a catastrophic event's occurrence, severity and timing are factors that we believe make it imprudent for a company to forecast and record an expected loss when the catastrophic event has not yet occurred. In addition, recording an expected loss for such a significant and uncertain event before it has occurred, adversely affected the policyholder, or before the loss could be practically estimated would not provide a faithful representation of an insurance contract's liability and is inconsistent with the "incurred loss" PAA model.

Example 13 of the Board's Proposed ASU requires establishment of an onerous contract loss for an expected catastrophic event, even if the catastrophic event does not occur. As a result, the onerous contract loss reserve would remain, with disclosure of updated assumptions and the status of the catastrophic event. We do not believe that having a significant loss recorded for an event that has not occurred as of the reporting period would provide a faithful representation of the insurance liability. Such a practice would lead to confusion and mislead financial statement users.

To illustrate how recognizing a loss due to a potential catastrophic event may impact our financial statements, we have provided an example based upon recent events. In late August 2011, there was an indication of a tropical storm occurring in the Atlantic. On August 30th, the National Oceanic and Atmospheric Administration forecasted this tropical storm would become a major hurricane ("Hurricane Katia") within the week. Based upon Hurricane Katia's prediction path, the southeast United States was at risk. At the end of August, models would have predicted that a category 3-4 hurricane hitting the Carolinas would result in a significant level of expected losses to Nationwide. Subsequent to August month end, it had become known that Hurricane Katia never made landfall in the United States. Therefore, if August were a reporting period, we believe that recording a material expected loss for Hurricane Katia, prior to it actually being incurred, would have significantly misrepresented Nationwide's insurance contract liabilities and financial performance, thus misleading financial statement users.

In addition to the concerns discussed above, we believe that current U.S. GAAP within ASC 855 (Subsequent Events) provides adequate guidance for the accounting and reporting of (1) additional information obtained or (2) significant events occurring subsequent to the reporting date. ASC 855-10-55-2 provides a specific example for a natural disaster (e.g., a hurricane) that occurs after the reporting date. ASC 855 (Subsequent Events) provides that a natural disaster occurring subsequent to a reporting date would not be recorded within the financial statements, but included as a disclosure (i.e., nonrecognized subsequent event). To alleviate the identified concerns within Example 13 of the Board's Proposed ASU discussed above, we propose that the Board maintains the practice within current U.S. GAAP, which requires losses to be recorded for catastrophic events only when the event has occurred, the event adversely affects the policyholder, and the loss can be reasonably estimated. Catastrophic events occurring after the reporting date will continue to be adequately accounted and reported for under ASC 855 (Subsequent Events).

Recognition of Expected Losses

The Proposed ASU requires expected losses to be recorded immediately in net income when the expected present value of the cash outflows exceeds the expected present value of cash inflows. Consistent with general loss criteria within current U.S. GAAP, we agree that expected losses should be recognized immediately. However, we believe that these expected losses should be based upon the actual economic nature of the insurance contract, and not an expected loss that results as a function of the BBA. For example, we have

concerns regarding potential loss recognition for certain spread-based annuity products (e.g., single premium immediate annuity) that will be within scope of the Proposed ASU. For those products, we have concerns that the BBA would preclude the inclusion of all expected investment earnings within the fulfillment cash inflows, as the discount rate determined in accordance with the Proposed ASU is not representative of an expected net earned rate (i.e., a pricing rate). As a result, spread-based annuity products, whose underlying profitability is highly dependent upon the investment earnings and interest credited to the policyholder, may result in an expected loss that is solely a function of the BBA, and does not indicate the actual underlying profitability of the contract. We recommend that the Board further consider those insurance contracts that will be measured under the BBA that may not include all the respective revenue streams that are integral to the economics of the insurance contracts. We believe that a final standard that results in the recognition of expected losses due to a function of the measurement model is inappropriate and will mislead financial statement users.

As previously discussed, we do not agree that an entity should discount the reserves (i.e., the liability for remaining coverage and liability for incurred claims) calculated under the PAA. Therefore, when facts and circumstances indicate that a portfolio of contracts may be onerous, we believe that the onerous contract test should be performed on an undiscounted basis, with the option to include expected investment income. This approach is consistent with current U.S. GAAP and considers a revenue stream that is integral in determining the pricing and profitability of an insurance contract. Therefore, exclusion of investment income when performing an onerous contract test may result in the recognition of expected losses for insurance contracts that are actually profitable, leading to confusion and information that is not useful to financial statement users.

If the Board decides to retain the requirement to discount the liability for remaining coverage and liability for incurred claims, we continue to have concerns about ignoring the impact of expected investment income in the onerous contracts test. We acknowledge that discounting the fulfillment cash flows already contains some impact of expected investment income. However, we believe that the proposed methods of determining the discount rate of the liability, as required by the Proposed ASU, do not capture the complete effect of expected investment income. Due to the importance of expected investment income in determining the profitability of an insurance contract, we believe that the requirement to exclude investment income would need to be reconsidered if the Board retains the discounting requirements.

Unlocking of the Margin

We do not agree with the approach to recognize changes in estimates of future cash flows in net income, a key difference between the Board and the IASB proposals, which will result in incomparable financial statements between companies that apply U.S. GAAP and International Financial Reporting Standards (“IFRS”). As the margin is measured as the difference between the present value of the fulfillment cash inflows and the present value of the fulfillment cash outflows, we view the margin as the expected profit of a portfolio of insurance contracts at its inception. However, locking the expected profit (i.e., margin) in at inception and over the life of the portfolio of insurance contracts presumes that an insurance company knows everything about the portfolio of insurance contracts, some of which have durations lasting several years. Given the uncertainty involved in measuring the profitability of an insurance contract, we do not believe it is appropriate to lock in an expected profit at inception and over the life of the portfolio of contracts. Therefore, we agree with the IASB’s decision to require unlocking of the margin to reflect changes in estimates of future cash flows.

Unlocking the margin to reflect changes in future estimated cash flows would provide a faithful representation of the expected profitability of an insurance contract and better portray the results of the business, by removing short-term volatility that is not reflective of the economics of the business. In addition, we believe that unlocking the margin will improve the proposed standard by removing the inconsistent treatment of measuring the margin at inception and over the life of the contract. For example, when changes in future estimated cash flows are favorable, immediate gains would be recognized within net income, which is conceptually inconsistent with the Proposed ASU, which prohibits the recording of gains at the initial

recognition of an insurance contract. In addition, the Proposed ASU requires immediate release of the remaining margin (i.e., recording of immediate gains) when a portfolio of insurance contracts is expected to generate an overall loss, but does not require adjustment of the margin when there are changes in estimated cash flows that impact the portfolio's expected profitability. The immediate recognition of the margin in a period in which a portfolio of insurance contracts is expected to generate a loss produces counterintuitive financial results, which will confuse financial statement users. We believe that adjusting the margin for changes in estimated future cash flows would faithfully represent the expected profitability of a portfolio of insurance contracts, produce consistent measurement of the contracts at inception and throughout the portfolio's life, remove volatility that is not reflective of the business results and eliminate the issue of producing counterintuitive results by recognizing immediate gains in periods when contracts are expected to generate a loss.

Although we support the IASB's decision to unlock the margin, we support doing so to allow for adjustment of the margin as if the change in estimated cash flows was known at the inception of the insurance contract. This approach will also have the effect of updating the future periods' margin release based on the updated assumption and is preferable to the method proposed by the IASB. Specifically, it will (1) provide a more faithful representation of the expected future profits (i.e., margin) of a portfolio of insurance contracts, and (2) demonstrate consistency with the BBA, which requires the updating of assumptions and cash flow estimates each reporting period. An example of our preferred approach is provided in Exhibit 1.

We acknowledge that a primary objective of the Board is to provide transparency in how an entity has performed in managing the risks associated with the assumptions that represent the core business of an insurance company. However, we do not believe that recognizing changes in assumptions that impact future estimated cash flows immediately through net income is the only way to provide transparency to financial statement users. We believe that the unlocking of the margin can be made transparent to financial statement users through an alternative presentation. This approach that illustrates on the Statement of Financial Position the change in the margin as a result of (1) changes in future estimated cash flows (i.e., the amount of margin unlocked in the period), and (2) margin recognized into insurance contract revenue. In addition, the Proposed ASU already includes enhanced disclosure requirements of the rollforward of the opening to closing balances of the insurance contract margin. If the margin were to be unlocked, this disclosure would capture the appropriate transparency by providing information on the assumption changes that impact future estimated cash flows. As a result, financial statement users will continue to be able to monitor the reliability of previous estimates.

Financial Statement Presentation

Overall Financial Statement Presentation

For insurance companies that issue life insurance or other long-term insurance contracts, we believe that the overall presentation requirements will not result in an improvement in decision-useful information over current U.S. GAAP. This information will lead to confusion in understanding insurance company financial statements and to increase usage of non-GAAP measures. The fundamental measurement of an insurance liability under the BBA is based upon an expected cash flow model. Therefore, we believe it is important that information presented within the financial statements provide a discernment of those cash flows, in order to understand the nature and economics of companies' insurance contracts. As discussed above, if the Board proceeds with the Proposed ASU, not only will the "potential" investors lack insights into the economics or management of the insurance business based on the financial statements, but the current financial statement users will also be negatively impacted.

If the Board continues to proceed to comprehensively change current U.S. GAAP, we believe that it is imperative that an alternative comprehensive presentation approach be developed that does not change how

insurance company financial statements are understood and more importantly that provides relevant and useful information that has the unanimous support of investors, analysts, management, preparers, and other financial statement users. Below we describe in further detail the most significant issues we have identified pertaining to financial statement presentation.

Revenue Recognition

We do not believe that insurance contract revenue, as defined within the Proposed ASU, faithfully represents the economics of an insurance company. Further, we do not believe it will provide relevant and decision-useful information to financial statement users. We acknowledge that the theoretical merit of the earned premium approach is based upon the principles of revenue recognition within current U.S. GAAP; however, we believe the life insurance industry is fundamentally different due to the long-term nature of its insurance contracts. The very nature of insurance contracts is the reason the Board has proposed separate accounting guidance from other revenue recognition principles. It is because of this difference that the concept of an “earned premium” has not historically been and will not become a relevant measure of performance for management, investors, analysts and other financial statement users. Therefore, the earned premium method for insurance contract revenue is materially different from what the financial statement users for insurance companies that issue life insurance or other long-term insurance contracts are accustomed to and will fundamentally change how these financial statements should be understood. Education efforts will be vast to help management, boards of insurance enterprises, analysts, ratings agencies and other key financial statement users to understand this new basis of accounting. Our belief is that this may result in an increased usage of unaudited non-GAAP measures for users to obtain the necessary information that is being successfully utilized today to evaluate and manage an insurance company. This comprehensive change in how an insurance company is viewed will result in significant incremental and ongoing costs that will have a downstream economic impact to preparers, policyholders, investors and other financial statement users.

We do not believe the Board’s proposed earned premium presentation approach, as well as the previously proposed summarized margin approach, will result in decision-useful information for financial statement users. Therefore, it is imperative for the Board to continue to obtain and analyze the feedback received from investors, analysts and other financial statement users to determine what information is relevant and useful in meeting the Proposed ASU’s objectives. If financial statement users find the “premium due” model to be most meaningful, then it should be retained. Adopting a standard that does not provide decision-useful information to financial statement users will result in significant incremental and ongoing costs without improving existing U.S. GAAP.

Segregated Fund Arrangements

The Proposed ASU’s requirement to present investment income on segregated fund accounts within the Statement of Comprehensive Income, separately from the interest expense representing the pass-through of that investment income, will lead to confusion for users of the financial statement. This will result in misleading yields on an insurance company’s assets that will not faithfully represent the investment performance of an insurance company. We believe that the current U.S. GAAP requirement to offset investment performance and the corresponding amounts credited to a contract holder would provide the most meaningful presentation to the financial statement users, as it allows users to readily analyze investment returns of an insurance company by excluding amounts earned on segregated fund assets that are fully passed through to policyholders and therefore not available to shareholders.

We believe the requirement to present investment income and the related pass-through is conceptually inconsistent with the asset management industry, which only requires the presentation of the fees earned and not the resulting investment income on assets managed and subsequent pass-through, and with accounting principles for a principal-agent relationship within the revenue recognition accounting literature. We believe

that the nature and economics of segregated fund arrangements currently within the insurance industry should be retained.

In addition, we believe that companies should have the option to present the liability for segregated fund arrangements within the insurance contract liability, or separately, on the Statement of Financial Position. Presenting segregated fund arrangements and the assets that support them separately from other items on the Statement of Financial Position better reflects the true risk to the insurance company.

Transition

Additional Time for Adoption

The most significant drivers affecting the implementation of the Proposed ASU include: current system constraints, historical information constraints and the development of processes and controls. Current systems are not equipped to handle the requirements of the Proposed ASU. Updating systems will require significant system modifications, and in many situations, development of new systems entirely. Historical information is maintained by most entities; however, the amount of historical information that is needed and maintained varies by entity. To implement the Proposed ASU accurately, the historical information will have to be accumulated, developed and reviewed. Also, public companies have filings with the Securities and Exchange Commission that include a five year financial information disclosure, which causes increased information needs and further complexities. Finally, as the Proposed ASU represents significant and fundamental changes to the insurance industry, new processes and controls will need to be developed, operationalized and monitored upon adoption and on a go-forward basis. Based on the above, we believe that the effective date of the Proposed ASU should not be earlier than six years after the issuance of the Proposed ASU. While we realize six years may seem to some as an unnecessarily long window for implementation, when compared with the typical two to three year window provided for other convergence projects, which are far less complex and represent far less of a comprehensive change as the Proposed ASU, we believe six years to be both a reasonable and necessary window.

Public versus Nonpublic Entity Considerations

We generally agree that the effective date of proposed guidance should be different for public and nonpublic entities. However, Nationwide has several public entities that are consolidated by nonpublic entities. In these cases, we believe companies should have the ability to adopt the Proposed ASU for the nonpublic entities, at the same time it is effective for the public entities. This will allow for consistency of application, stream-lined reporting and implementation activities and less confusion for financial statement users of both sets of financial statements.

Consideration of Known Events in the Retrospective Adoption of the Proposed ASU

We appreciate the Board's efforts to make the transition guidance of the Proposed ASU as operational as possible with the use of practical expedients (e.g., determining of portfolios at transition). However, given the operational challenges in determining the margin at transition, even utilizing the practical expedients provided, we strongly encourage the Board to consider allowing preparers the option to use the practical expedient provided in the proposed IASB standard, as outlined in paragraphs C5 and C6, which allows the ability to use the benefit of hindsight in determining the cash flows necessary to determine the margin at the transition date. We believe that using hindsight to consider what has actually occurred at transition would not only alleviate significant operational burdens for preparers to gather historical assumptions, but would also greatly improve both verifiability and comparability, while still providing a margin at transition that faithfully represents the profit remaining for the contracts in force upon transition.

While we understand there may be conceptual concerns with using hindsight for determining the margin at transition, as it is the equivalent of having “unlocked” the margin between inception and the transition date, we believe that such treatment is warranted in these circumstances. We believe a margin calculated in this way provides a more relevant measure to financial statement users than defaulting to a zero margin if the necessary information is unavailable, while providing potentially significant cost savings related to the transition portion of the guidance.

CONCLUSION:

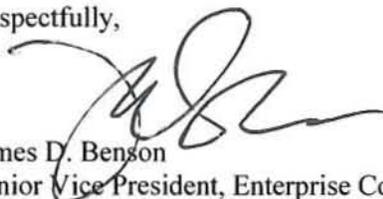
We have significant concerns that the proposed measurement model will not provide relevant information that will help users of an entity’s financial statements make sound economic decisions. While we are supportive of the overall objectives of the project to improve current U.S. GAAP, provide investors with decision-useful information, and achieve convergence with the IASB, we do not believe that a comprehensive reconsideration of current U.S. GAAP is necessary since full convergence with the IASB has not been achieved. Although the Board and the IASB have reached agreement on many principles to develop a “mostly” converged standard, material differences within the fundamental measurement model are highlighted throughout the comment letter and in the Appendix. They include, but are not limited to, the use of a single margin versus a dual margin approach, locking versus unlocking of the margin, and the types of costs included within the fulfillment cash flows (including the accounting for direct acquisition costs) and remain unresolved. Since the Board and the IASB have been unable to reconcile these material differences, the standards will produce vastly different results, thus leading to concerns regarding the comparability of U.S. and International insurance companies. Further, we encourage the Board to continue to weigh the costs for each of the proposed decisions in correlation with the overall benefit to the financial statement users, to determine if the added complexity is justified, as the costs associated with implementing this new standard will be significant and will ultimately impact the policyholders of the insurance contracts.

Before the Board finalizes a standard, we believe that it is imperative for the Board to continue to utilize the feedback received from current and “potential” investors, analysts and other financial statement users. We believe that if further outreach is performed, the Board will see that the overwhelming opinion of the industry and financial statement users is that the Proposed ASU does not result in decision-useful information and would represent a setback from current U.S. GAAP.

Additionally, we have attached Nationwide’s response to the comprehensive listing of questions asked by the Board as an appendix to this letter.

We hope these comments assist you during your re-deliberations of the Proposed ASU. In the event that any Board or staff member would like further clarification of our positions, we would be happy to explain them in greater detail.

Respectfully,



James D. Benson
Senior Vice President, Enterprise Controller and Chief Accounting Officer
Nationwide and Subsidiaries

Exhibit 1:

Below is an example of our preferred approach for unlocking the margin.

For reference purposes, below is a table depicting an example of an original cash flow estimate:

	0	1	2	3	4	5	6	7	8	9	10
Premiums		100	100	100	100	100	100	100	100	100	100
Claims		75	75	75	75	75	75	75	75	75	75
Liability at End of Period	750	675	600	525	450	375	300	225	150	75	0
Margin Recognized		25	25	25	25	25	25	25	25	25	25
Margin at End of Period	250	225	200	175	150	125	100	75	50	25	0

Assume at the end of year 8, the company updates its assumptions and had different claims expectations in year 9 and 10 of \$25 per year (i.e., all other assumptions stay constant).

For reference purposes, below is a table depicting the updated cash flow estimate, as if the change was known at inception:

	0	1	2	3	4	5	6	7	8	9	10
Premiums		100	100	100	100	100	100	100	100	100	100
Claims		75	75	75	75	75	75	75	75	25	25
Liability at End of Period	650	575	500	425	350	275	200	125	50	25	0
Margin Recognized		35	35	35	35	35	35	35	35	35	35
Margin at End of Period	350	315	280	245	210	175	140	105	70	35	0

Below is a table depicting how our recommended approach impacts the year of change and on a go-forward basis when unlocking the margin:

	0	1	2	3	4	5	6	7	8	9	10
Premiums		100	100	100	100	100	100	100	100	100	100
Claims		75	75	75	75	75	75	75	75	25	25
Liability at End of Period	750	675	600	525	450	375	300	225	50	25	0
Margin Recognized		25	25	25	25	25	25	25	105	35	35
Margin at End of Period	250	225	200	175	150	125	100	75	70	35	0

APPENDIX

Scope

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

No. We are supportive of including all entities that issue insurance contracts, unless those contracts are provided specific scope exceptions. However, we believe the scope exceptions should be modified as follows:

- We believe that all financial guarantees, guarantees on securitized assets, indemnities, sale guarantees, representations and warranties should be excluded from the scope of the Proposed ASU. These contracts do not meet the spirit of the Proposed ASU and we believe the current U.S. GAAP guidance for these items, such as contingency guidance, is appropriate and has resulted in proper accounting for these risks.*
- Certain features, such as roadside assistance and credit monitoring, can be included in property & casualty insurance contracts. We understand that some companies believe these types of features should be in the scope of the Proposed ASU, while others believe they should not be, and that the Board has debated this topic to help ensure consistent application. Although we generally support the criteria that should be considered to determine whether a distinct good or service exists, we believe that the criteria could cause an issue with these types of features when they are applied to insurance entities. Because these items are generally sold independently by other companies not in the insurance industry, we are concerned that some insurers may account for these features separately and others may not. As an insurer does not sell these features without an insurance contract and they are not distinct from the insurance contract, we believe that insurance entities should always consider these features part of the insurance contract. This will help ensure the industry is considering these features consistently and will enhance comparability from insurer to insurer.*

Recognition

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

Yes. We agree with the requirements included in the Proposed ASU that require embedded derivatives, distinct investment components and distinct performance obligations to provide goods or services to be separated and accounted for under other applicable Topics. We believe these requirements aid in providing transparency into the components of an insurance contract that do not respond to changes in circumstances in the same manner as components affected by insurance risk and will provide comparability with other non-insurance type contracts, such as financial instruments issued by banks, that are similar in nature. However, if the Proposed ASU is adopted, we recommend the final guidance provide additional clarity through the use of examples in application of the unbundling guidance, to avoid confusion and divergence of industry practice that would result in a lack of comparability. For example, it is particularly unclear how the unbundling of certain performance obligations, such as investment management services, would apply to life insurance type products. In addition, we believe it is particularly unclear what types of fulfillment cash flows would be considered within these investment management services. For example, certain types of fees within our products, such as those for mortality and expense risks, administrative expenses, and mutual fund revenues (i.e., fees from revenue sharing contracts) are an integral part of providing insurance coverage. Therefore, we do not believe cash flows for these types of

services, for any products within the scope of the insurance contracts standard, should be unbundled, as those services are an integral part of providing insurance coverage. Alternatively, if these types of services were unbundled and accounted for under revenue recognition guidance, this would likely result in the inappropriate recognition of losses as onerous contracts, as these fees are a significant source of revenue for many insurance products (e.g., variable annuities, universal life insurance, etc.). Similar to the concerns outlined in our response to question 24, we believe it would be inappropriate to record losses that result as a function of the measurement models within the Proposed ASU, and not the actual economic nature of the insurance contract.

Initial and Subsequent Measurement

Question 3: Will the proposed measurement model produce relevant information that will help users of an entity's financial statements make economic decisions? If not, what changes do you recommend and why?

No. As discussed within the comment letter and in other questions within this Appendix, we have significant concerns that the proposed measurement model will not provide relevant information that will help financial statement users make economic decisions. While we are supportive of the overall objectives of the project to improve current U.S. GAAP where improvements may be warranted, provide investors with decision-useful information, and achieve convergence with the IASB, we do not believe that a comprehensive reconsideration of current U.S. GAAP is necessary, especially since full convergence with the IASB has not been achieved. Although the Board and the IASB have reached agreement on many principles to develop a "substantially" converged standard, material differences within the fundamental measurement model remain unresolved, including the use of a single margin versus a dual margin approach, locking versus unlocking of the margin and the types of costs included within the fulfillment cash flows (including the accounting for direct acquisition costs). Since the Board and the IASB have been unable to reconcile these material differences, the standards will produce vastly different results, thus leading to concerns regarding the comparability of U.S. and International insurance companies. In addition to these concerns on comparability, failure to achieve a single accounting standard for insurance contracts will result in significant costs incurred by companies that report on both U.S. GAAP and IFRS to maintain multiple accounting systems and apply multiple processes to support reporting on both bases of accounting.

Although there are areas within current U.S. GAAP that can be improved, we do not support a comprehensive reconsideration of the current accounting standard, especially with a new standard that has not met all of the key objectives of the proposal. We believe the fundamental changes within the Proposed ASU do not result in an improvement in decision-useful information over current U.S. GAAP and will require enormous education efforts to help management, boards of insurance companies, analysts, ratings agencies and other key financial statement users understand this new basis of accounting. The presentation requirements will result in the obscurity of information and increased confusion in regards to how insurance companies are managed. The fundamental measurement of an insurance contract liability under the BBA is based upon an expected cash flow model; however, the presentation requirements under the Proposed ASU do not provide an understanding of those cash flows or of the underlying nature and economics of the company's insurance contracts. We believe the result of providing information that is not decision-useful to financial statement users will result in an increased use of non-GAAP measures to obtain the necessary information that has been historically utilized to evaluate and manage insurance companies. Therefore, we would challenge the assertion that the Proposed ASU will provide relevant information that will help financial statement users in making economic decisions.

We believe it is imperative for the Board to continue to utilize the feedback received from investors, analysts and other financial statement users to determine whether the Proposed ASU meets one of its key objectives to provide decision-useful information that represents an improvement to current U.S. GAAP. We respectfully request the Board weigh the significant economic impact to preparers of the financial statements to implement these fundamental changes, as well as the resulting downstream impact to policyholders, investors, analysts and other financial statement users. A key objective of the Proposed ASU is to provide comparability amongst companies

(e.g., U.S. and International insurance companies), and since the Board and the IASB have been unable to achieve a fully converged standard, we recommend the Board specifically identify those areas within current U.S. GAAP that can be improved and focus on those targeted areas for enhancement. We believe this will help maintain a standard that provides financial statement users the necessary information to evaluate and analyze the insurance business, without the fundamental changes that would have a significant downstream economic impact to preparers and financial statement users.

Question 4: Which aspects of the proposed measurement model most significantly improve the information that will be used in making economic decisions and why?

While we agree with many of the concepts underlying the Proposed ASU and we acknowledge certain aspects of the guidance have well-reasoned and theoretical merit, we do not believe the Proposed ASU will result in improved information that will be used in making economic decisions by financial statement users. As discussed within the comment letter and our responses to questions 31 and 40, we have significant concerns with the overall presentation approach within the Proposed ASU. We do not believe the presentation requirements of the Proposed ASU will appropriately reflect the underlying measurement model for an insurance contract liability. Additionally, while we can appreciate the Board's rationale for measuring investment returns separately from insurance contract liabilities, ignoring the linkage between the expected investment returns and the pricing of the insurance contracts through the premium charged will result in a misleading and unfaithful representation of the insurance liability. While we have not provided the Board with areas where we believe targeted improvements to existing U.S. GAAP may be warranted, we acknowledge that the Board identified a number of areas within the Proposed ASU where targeted improvements to existing U.S. GAAP may be justified. We believe that the Board could provide a greater benefit to the financial statement users at a lower cost if targeted improvements to current U.S. GAAP were pursued, as opposed to a full replacement of the accounting for insurance contracts with the Proposed ASU. We would appreciate the opportunity to discuss those areas and potentially others with the Board further, if the Board decides to take our recommendation and further pursue this approach instead of the Proposed ASU.

We appreciate the Board's significant efforts to work with the IASB towards developing a high quality insurance accounting standard, and we are supportive of the key objectives of the Proposed ASU to increase comparability among companies that issue insurance contracts, provide decision-useful information to financial statement users and reach a converged standard that would benefit the competitive marketplace and investment community on a global basis. However, as the Board and the IASB have not been able to reach full convergence, we do not believe the Proposed ASU has met these key objectives. The proposed measurement model will result in less useful information to financial statement users, without alleviating concerns of comparability among U.S. and International insurance companies. Therefore, we are not supportive of the Proposed ASU and we do not believe the proposal will improve information that is currently provided to financial statement users under U.S. GAAP.

As discussed in our response to question 3, we recommend the Board specifically identify those areas within current U.S. GAAP that can be improved and focus on those targeted areas for enhancement.

Measurement Approaches

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

Yes. We support the use of a two-model approach for insurance contract accounting. The business models for property and casualty insurance and life insurance are fundamentally different and as such warrant different accounting.

Question 6: Do you agree that entities should be required to apply the premium allocation approach if the coverage period of the insurance contract, considering the contract boundary guidance, is one year or less? If not, what would you recommend and why?

Yes. This would facilitate better comparability of financial statements across the marketplace.

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

No. While we agree with the proposal to provide a different approach for the measurement of short-duration contracts, we do not believe this criterion is defined appropriately. Based on the Background Information, Basis for Conclusions and Alternative Views (“the Basis for Conclusions”), we believe the intent of the criterion was to limit the use of the PAA model to contracts for which updating assumptions before a claim is incurred would not provide much more meaningful information to financial statement users (most short duration contracts under existing U.S. GAAP). However, through discussion with industry peers, we have encountered widely differing interpretations of how this criterion would be applied. For instance, although the Basis for Conclusions discusses catastrophes and that the criterion was not intended to capture these risks, we believe the words still encompass these risks. Furthermore, the requirement to adjust the financials for such risks before the claim is incurred through the onerous contracts provision would seem to make it difficult to support the idea that significant variability in the expected net cash flows is unlikely before a claim is incurred for future contracts covering similar risks. Another example of where this criterion is complex to apply is surety contracts. The Proposed ASU provides an example of a 3-year surety contract that would be accounted for under the PAA when the contractor’s financial position is stable and the contractor has historically completed construction contracts on time. However, if these facts are not true, we don’t believe that it should change the accounting for these contracts.

Portfolio and Contract Boundary

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

No. In general, we support principles-based definitions; however, we believe that the definition of a portfolio should center on how the business is managed, since that factor most significantly affects how a company is differentiated and derives value and as such should underlie the measurement of a company’s insurance contracts to create decision-useful information. Current U.S. GAAP requires an insurance company to group its contracts consistent with its manner of acquiring, servicing and measuring the profitability of its insurance contracts. This requirement acknowledges the linkage between the definition of a portfolio and how the insurance contracts are being managed as a group. Although we believe this definition has stood the test of time, we acknowledge that the Board wants to update it. As such, we believe the definition of a portfolio should be modified to group insurance contracts that are “managed together as a single pool.” Indicators that the insurance contracts are managed together as a single pool may include that they are subject to similar risks, expected to have similar patterns of release from risk, priced similarly relative to the risk assumed, or priced together.

As proposed, the definition of portfolio is not aligned with the manner in which insurance companies manage their business, which will significantly increase the cost of implementing and the complexity of applying this standard. We believe this added complexity will ultimately result in differences in application among companies. We have concerns with this definition due to the unintended consequences it has on all aspects of the model (e.g., onerous contracts, margin and discount rate determination, etc.). We believe that if the criterion is left as currently proposed, the result will be insurance companies tracking a voluminous number of portfolios.

While we are concerned with the overall proposed definition of portfolio, we have significant concerns regarding the duration requirement in particular and the impact on contracts with multiple perils. The duration requirement seems to suggest that an entity could not combine life insurance policies issued to thirty-year olds and fifty-year olds that are exactly the same, because different age groups may have different expected durations. Further, it would seem the duration requirement would force companies to bifurcate multiple peril insurance contracts (e.g., physical damage versus liability, etc.) due to different durations for these perils. As the definition refers only to groupings of contracts, not portions of contracts, we believe the intention is not to require bifurcation at this level into separate portfolios.

The permutations of these proposed criteria (subject to similar risks, priced similarly relative to the risks assumed, similar duration, and similar patterns of release from risk) will force companies to an undue level of granularity, which will exacerbate the costs of applying this standard and lead to less meaningful results. For example, a focus on pricing with no consideration of the diversification strategies management has put in place ignores a core fundamental of the insurance business model. We believe modifying the proposed portfolio definition as discussed above will allow companies to measure their contracts in a manner which more faithfully represents how the business is managed, providing financial statement users with reliable and relevant financial information while reducing the costs of applying the Proposed ASU.

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

Yes.

Fulfillment Cash Flows

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

No. We do not agree with the types of cash flows that would be included in the measurement of fulfillment cash flows within the Proposed ASU. We believe the types of cash flows that should be included within the insurance liability measurement is a fundamental area within the BBA that requires convergence with the IASB. We support the IASB's approach that includes all cash outflows that arise directly from an insurance contract or can be attributed to them on a reasonable and consistent basis. We believe all cash flows that are expected to arise as a company fulfills the insurance contract liability should be treated in the same way and not distinguished on the basis on which they occur or on the basis of who the counterparty is. As a result, the IASB's approach has the effect of including direct acquisition costs, such as commissions and transaction based taxes, which are specifically excluded from the fulfillment cash flows under the Board's approach. As discussed in question 13, we view the margin as the expected profit of a portfolio of insurance contracts. As cash flows for direct acquisition costs are factored into the determination of an insurance contract's expected profitability, we believe inclusion of these expected costs within the fulfillment cash flows would provide a more meaningful representation of the margin that will be recognized over the remaining coverage and claims settlement periods.

In addition, we also recommend that the measurement model include "other assessments" as allowed in ASC 944-30-35-5, so revenue-sharing contracts with underlying mutual funds may be considered within the fulfillment cash flows.

We do support the inclusion of cash flows related to embedded options and guarantees related to insurance coverage that are not separated and accounted for as embedded derivatives.

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

No. We believe that assumptions used in the measurement of fulfillment cash flows should be updated when actual experience or other evidence suggests the assumptions should be revised. We acknowledge the concern within current U.S. GAAP for traditional long duration insurance contracts (e.g., whole life insurance), which requires the assumptions for these types of insurance contracts to be locked in at inception unless the portfolio is subsequently determined to be in a loss position. We agree that assumptions used in the measurement of fulfillment cash flows should be updated; however, we do not believe updating the assumptions each reporting period is prudent based upon the long-term nature of these contracts. The requirement that such business be valued each reporting period using updated assumptions may lead to additional volatility within net income that is not representative of the true economics of this relatively stable, long-term business. Assumptions are developed based upon management's business model, including the long-term nature of the underlying liabilities for these insurance contracts. Based upon historical experience, assumptions within these liabilities remain relatively consistent and do not significantly change each reporting period. Therefore, we do not support a requirement to update all assumptions used in the measurement of the fulfillment cash flows each reporting period. In addition, the incremental costs for enhanced processes, controls and efforts to support the updating of assumptions each reporting period for these long-term contracts do not outweigh the perceived benefit of providing a current view of these traditional insurance contract liabilities, which do not significantly fluctuate as a result of changes in assumptions used in measuring fulfillment cash flows each reporting period.

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

No. To satisfy the intent of the proposed measurement model, we propose further guidance and clarification to specifically support current actuarial methods and concepts, such as the "actuarial central estimate" utilized today within the property and casualty insurance industry. We share the significant concern of the actuarial community with the verbiage "unbiased probability weighted estimate" included in the Proposed ASU and with the practical implications of how that may be applied to insurance contracts under the PAA. It could be interpreted that the ability of an actuary to weigh the scenarios in the methodology used would indicate that an estimate can never be truly "unbiased." In addition, some in the industry believe that to comply with this requirement, a purely statistical method would need to be established; however, such an approach would be overly restrictive and inconsistent with best practice.

We believe that the best description of property and casualty cash flow estimates may be derived from the current guidance promulgated by the American Academy of Actuaries' Actuarial Standards Board, in their publication titled ASOP 43. This publication describes the actuarial central estimate as "an estimate that represents an expected value over the range of reasonably possible outcomes." ASOP 43 provides further clarification that "an actuarial central estimate may or may not be the result of the use of a probability distribution or a statistical analysis. This description is intended to clarify the concept rather than assign a precise statistical measure, as commonly used actuarial methods typically do not result in a statistical mean."

We believe it is not the Board's intention to comprehensively change current and historically proven actuarial methods, but rather to remove unsupported management estimates and ensure that liabilities are measured based on established actuarial principles. Likewise, we believe the Board seeks to require appropriate rationalization and support for any management adjustments to these actuarially determined values. We request that the Board clarify the intention of the guidance, to (1) specifically support actuarial methods and actuarial standards of

practice currently in use today within the property and casualty industry, and (2) allow management adjustments to the actuarially determined expected values with appropriate rationalization and support, based upon management's expertise and thorough understanding of the business. We do not believe it appropriate to require that a statistical modeling approach be used to derive loss reserve estimates, as that approach has not been proven to be sufficiently reliable or accurate and would potentially preclude the incorporation of vital qualitative information from the reserving process, resulting in diminished accuracy. It also would result in a fundamental change in how the claims reserving process is understood by analysts and other financial statement users, would limit the use of historically proven actuarial methods, and would result in a significant change in claims reserving practices for the property and casualty insurance industry.

For life and other long-term insurance contracts that apply the BBA, if it is the Board's intention to allow only a stochastic modeling approach to derive a purely statistical mean for determining fulfillment cash flows, this will consequently provide less decision-useful information and affect the comparability of insurance contract liabilities between companies, due to the increased usage of standard scenario generators that will not be dictated. To meet the Proposed ASU's key objectives of increasing comparability and providing decision-useful information, we support the use of deterministic models, when appropriate, which will provide increased comparability and transparency in the liability measurement for insurance contracts.

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

No. We do not agree with the approach to recognize changes in estimates of future cash flows in net income, a key difference between the Board and the IASB proposals, which will result in incomparable financial statements between companies that apply U.S. GAAP and IFRS. As the margin is measured as the difference between the present value of the fulfillment cash inflows and the present value of the fulfillment cash outflows, we view the margin as the expected profit of a portfolio of insurance contracts at its inception. However, locking the expected profit (i.e., margin) in at inception and over the life of the portfolio of insurance contracts presumes that an insurance company knows everything about the portfolio of insurance contracts, some of which have durations lasting several years. Given the uncertainty involved in measuring the profitability of an insurance contract, we do not believe it is appropriate to lock in an expected profit at inception and over the life of the portfolio of contracts. Therefore, we agree with the IASB's decision to require unlocking of the margin to reflect changes in estimates of future cash flows.

Unlocking the margin to reflect changes in future estimated cash flows would provide a faithful representation of the expected profitability of an insurance contract and better portray the results of the business, by removing short-term volatility that is not reflective of the economics of the business. In addition, we believe that unlocking the margin will improve the proposed standard by removing the inconsistent treatment of measuring the margin at inception and over the life of the contract. For example, when changes in future estimated cash flows are favorable, immediate gains would be recognized within net income, which is conceptually inconsistent with the Proposed ASU, which prohibits the recording of gains at the initial recognition of an insurance contract. In addition, the Proposed ASU requires immediate release of the remaining margin (i.e., recording of immediate gains) when a portfolio of insurance contracts is expected to generate an overall loss, but does not require adjustment of the margin when there are changes in estimated cash flows that impact the portfolio's expected profitability. The immediate recognition of the margin in a period in which a portfolio of insurance contracts is expected to generate a loss produces counterintuitive financial results, which will confuse financial statement users. We believe that adjusting the margin for changes in estimated future cash flows would faithfully represent the expected profitability of a portfolio of insurance contracts, produce consistent measurement of the contracts at inception and throughout the portfolio's life, remove volatility that is not reflective of the business results and eliminate the issue of producing counterintuitive results by recognizing immediate gains in periods when contracts are expected to generate a loss.

Although we support the IASB's decision to unlock the margin, we support doing so to allow for adjustment of the margin as if the change in estimated cash flows was known at the inception of the insurance contract. This approach will also have the effect of updating the future periods' margin release based on the updated assumption and is preferable to the method proposed by the IASB. Specifically, it will (1) provide a more faithful representation of the expected future profits (i.e., margin) of a portfolio of insurance contracts, and (2) demonstrate consistency with the BBA, which requires the updating of assumptions and cash flow estimates each reporting period. An example of our preferred approach is provided in Exhibit 1.

We acknowledge that a primary objective of the Board is to provide transparency in how an entity has performed in managing the risks associated with the assumptions that represent the core business of an insurance company. However, we do not believe that recognizing changes in assumptions that impact future estimated cash flows immediately through net income is the only way to provide transparency to financial statement users. We believe that the unlocking of the margin can be made transparent to financial statement users through an alternative presentation. This approach that illustrates on the Statement of Financial Position the change in the margin as a result of (1) changes in future estimated cash flows (i.e., the amount of margin unlocked in the period), and (2) margin recognized into insurance contract revenue. In addition, the Proposed ASU already includes enhanced disclosure requirements of the rollforward of the opening to closing balances of the insurance contract margin. If the margin were to be unlocked, this disclosure would capture the appropriate transparency by providing information on the assumption changes that impact future estimated cash flows. As a result, financial statement users will continue to be able to monitor the reliability of previous estimates.

Discount Rate and Discounting

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

No. We believe the discount rates used by the entity for nonparticipating contracts should reflect the characteristics of the insurance contract liability or those of the assets backing that liability based on the management of the business. A significant portion of insurance business consists of long-term liabilities that are priced and managed in concert with the assets backing them, in order to provide for the ultimate cash flows along with a provision for profit. As such, we believe the interest rate, explicit or implicit, used in the pricing of an insurance contract would generally be the appropriate discount rate, as this rate reflects the characteristics of the insurance contract liability that can be observed at the time of issuance. When an asset liability management strategy is being adhered to, this rate would be similar or identical to the expected earned rate on the assets backing the contract, net of expected default losses. The pricing rate is reflected directly in the premiums charged to the customer and is a rate that would prevent losses (or a significantly reduced margin) at inception for portfolios of contracts that are expected to be profitable overall. Therefore, it reflects the most likely outcome of the insurance activity as a whole, considering the underwriting and investment function together.

We understand the Board may be concerned about using a pricing rate in the current fulfillment model, as rates may have significant movements in the days following the sale of the insurance contract. However, we believe that such movements could be taken into consideration through an update, to reflect the interest rate used in pricing new insurance contracts with similar features. In the absence of unusual pricing or investment activity, the updated pricing rate is likely to continue to be the future expected earned rate, but be measured as of that new point in time. To the extent interest rates have moved in the interim, the asset fair values would have moved accordingly, and the expected earned rate from those assets would have changed appropriately to reflect the changed economic environment.

We recognize that there may be unusual situations that would not support the presumption that the pricing rate (i.e., the expected earned rate adjusted for defaults) represents a rate that reflects the characteristics of the liability. Examples of when using a pricing rate would be inappropriate would be an entity under-pricing the market to gain market share or over-pricing the market to effectively leave a market. Indicators could be provided by the Board for insurers to use to assess if their own expected asset earned rate is not consistent with the characteristics of the insurance contract liability. One indicator may be if the entity's prices are out of line with competitors' prices for similar products, or if its prices are out of line with reinsurance prices for ceding similar risks. However, in the absence of evidence to the contrary, the rebuttable presumption should be that the insurer's own expected earned rate, net of expected defaults, reflects the rate consistent with the characteristics of the insurance contract liability.

By not considering the rate used to price the insurance contract, a complete picture of the company's financial results cannot be seen, which results in less relevant financial information. Ultimately, disregarding the critical inter-relationship between assets backing insurance liabilities in determining the discount rate to be used in the measurement of those liabilities would be to the detriment of the financial statement users and would make U.S. GAAP reporting significantly less meaningful to management.

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

No. While we understand the theoretical merit of considering the time value of money as it relates to the fulfillment of insurance contract liabilities, we do not agree that an entity should discount the reserves (i.e., the liability for remaining coverage and liability for incurred claims) calculated under the PAA model. Discounting requires the estimation of both the amount and timing of cash flows. In the property and casualty business, where most contracts would follow the proposed PAA model, the timing of the cash flows is uncertain, unlike a life insurance contract where the benefits are able to be modeled. Discounting reflects the time value of money, but ignores the risk of uncertainty in the cash flows and additionally introduces new interest rate risk to the balance sheet. Discounting these reserves may also give financial statement users a false sense of confidence in an insurer's ability to estimate the timing of these reserves. This creates comparability issues between companies and will provide less decision-useful information to the financial statement users. Further, the current standard of not discounting the reserves provides an implicit risk margin for the reserves. We believe this is prudent given the complexities in the estimation process, as well as the inherent unknowns associated with the timing of payments. Though an imprecise risk margin, this standard is well established in both U.S. GAAP and statutory accounting and consequently understood by analysts, existing and potential investors, regulators and other financial statement users.

Furthermore, as we do not support discounting for contracts measured under the PAA, we are not promoting the combination of discounting and the use of a separate explicit risk margin. Such an approach would add significant cost and uncertainty and not be viewed as an improvement over current practice. An explicit risk margin would not be able to be reliably calculated and its use would make published financial results less transparent and comparable.

Finally, based on discussions with analysts and other financial statement users, users will not use the discounted amounts; rather, they will adjust those amounts back to the undiscounted liability amounts. We understand that the Board believes that the analysts and users will become accustomed to the financial statements in the manner required under the Proposed ASU. However, we believe that this perception is not focused on what the user community wants. We believe that discounting has resulted in a failed attempt at transparency in the past (e.g., pension accounting), and we do not want to see that happen for reserves associated with the PAA. The liability for remaining coverage and the liability for incurred claims should be measured in a manner that is useful to the

financial statement users. It's true that discounting the liabilities would provide financial benefit to companies utilizing the PAA through bolstering capital and reducing liabilities, but the industry believes so strongly that discounting under the PAA will not provide more relevant information to the financial statement users that the industry is looking beyond this benefit, to reflect what we believe to be a more appropriate representation of our liabilities to policyholders.

We believe retaining this requirement will result in significant implementation costs and financial statements that are less comparable, decision-useful and relevant than financial statements under existing accounting standards..

We do not support the discounting requirement for contracts accounted for using the PAA, as we believe reflecting discounting as proposed would result in a less than faithful representation of our liabilities. As an alternate approach, though, if done at an appropriate level, we would support providing a sensitivity analysis for contracts accounted for using the PAA. As stated above, we agree with the theoretical merit of considering the time value of money, but due to the nature of the liabilities to be accounted for using the PAA, we believe this consideration would be more meaningful and relevant when provided as a range of possible discount rate impacts. Additionally, this alternative would significantly reduce the costs of applying this standard.

Finally, if the Board moves forward with discounting, we believe that the Board should allow the use of a risk-free rate alone to discount these reserves. Although the risk-free rate will not contain all of the characteristics inherent in the reserves, it will be the most significant component of the discount rate, especially as it pertains to contracts accounted for under the PAA, which would generally be thought to have less illiquidity than those contracts accounted for under the BBA. As the discount rate will be less than the method prescribed under the Proposed ASU, it will inherently incorporate a risk adjustment in the amount and will result in higher reserves. Further, as the development of the liquidity premium added to the risk-free rate involves more judgment, eliminating the liquidity adjustment from the discount rate development would promote consistency and comparability among companies required to discount using the PAA.

Question 16: Do you agree that an entity should segregate the effects of underwriting performance from the effects of changes in discount rates (which would reverse over time) by recognizing changes in the present value of the fulfillment cash flows due to changes in the discount rates in other comprehensive income? If not, do you think that the effect of changes in the discount rates should be presented in net income? Please explain your reasoning.

Yes. We agree that an entity should be given the ability to segregate the effects of underwriting performance from the effects of changes in discount rates, by recognizing changes in the present value of fulfillment cash flows due to changes in the discount rates in other comprehensive income. However, as mentioned previously, a significant portion of insurance business consists of long-term liabilities that are priced and managed in connection with the assets backing them, in order to provide for the ultimate cash flows along with a provision for profit. Other portfolios of insurance business are more market-sensitive and may be managed as such. Therefore, we believe the accounting for insurance contracts should be done in a manner consistent with how the business is managed. If liabilities and assets are being managed together, they should be accounted for consistently, whether that is through net income or other comprehensive income. As such, we believe companies should have the flexibility to elect to present all changes in the liability (inclusive of changes in the discount rate) in net income if it would eliminate a significant accounting mismatch. To ensure comparability from company to company, added disclosures may need to be considered.

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

No. We do not believe that a test should be required to trigger recognition in net income of some or all of the amounts in accumulated other comprehensive income. Although we can conceptually understand the merits of this concept similar to other than temporary impairment, we believe there is minimal benefit to be gained, and it would add an additional layer of complexity and costs to an already complex model. For fully guaranteed contracts, such a test would over-complicate the model for changes that automatically reverse over time. For other contracts with participation features that are discretionary, there is no such need for a loss recognition test, as the asset-liability mismatch is already reflected in the measurement. Further, the disclosures included in the Proposed ASU more than adequately address this risk.

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

Yes. We agree that the approach for calculating the discount rates should not be prescribed by the Proposed ASU, but rather determined using a principles-based approach. Depending on the company and its asset and liability management processes, a principles-based approach would provide companies with the flexibility to apply the guidance consistently with how they manage their business. A significant portion of insurance business consists of long-term liabilities that are priced and managed in concert with the assets backing them, in order to provide for the ultimate cash flows along with a provision for profit. As such, we believe the interest rate, explicit or implicit, used in the pricing of an insurance contract would generally be the appropriate discount rate, as this rate reflects the characteristics of the insurance contract liability that can be observed at the time of issuance. When an asset liability management strategy is being adhered to, this rate would be similar or identical to the expected earned rate on the assets backing the contract, net of expected default losses. The pricing rate is reflected directly in the premiums charged to the customer and is a rate that would prevent losses (or a significantly reduced margin) at inception for portfolios of contracts that are expected to be profitable overall. Therefore, it reflects the most likely outcome of the insurance activity as a whole, considering the underwriting and investment function together.

We understand the Board may be concerned about using a pricing rate in the current fulfillment model, as rates may have significant movements in the days following the sale of the insurance contract. However, we believe that such movements could be taken into consideration through an update, to reflect the interest rate used in pricing new insurance contracts with similar features. In the absence of unusual pricing or investment activity, this rate is likely to continue to be the future expected earned rate, but be measured as of that new point in time. To the extent interest rates have moved in the interim, the asset fair values would have moved accordingly, and the expected earned rate from those assets would have changed appropriately to reflect the changed economic environment.

We recognize that there may be unusual situations that would not support the presumption that the pricing rate (i.e., the expected earned rate adjusted for defaults) represents a rate that reflects the characteristics of the liability. Examples of when using a pricing rate would be inappropriate would be when an entity under-prices the market to gain market share or over-prices the market to effectively leave a market. Indicators could be provided for insurers to use to assess if their own expected asset earned rate is not consistent with the characteristics of the insurance contract liability. One indicator may be if the entity's prices are out of line with competitors' prices for similar products, or if its prices are out of line with reinsurance prices for ceding similar risks. However, in the absence of evidence to the contrary, the rebuttable presumption should be that the insurer's own expected earned rate, net of expected defaults, reflects the rate consistent with the characteristics of the insurance contract liability.

By not considering the rate used to price the insurance contract, a complete picture of the company's financial results cannot be seen, which results in less relevant financial information. Ultimately, disregarding the critical inter-relationship between assets backing insurance liabilities in determining the discount rate to be used in the

measurement of those liabilities would be to the detriment of the financial statement users and would make U.S. GAAP reporting significantly less meaningful to management.

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

Yes.

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

No. We agree that upon any change in expectations of the crediting rates used to measure the insurance contract liability for insurance contracts with discretionary participation features, the interest accretion rates should be reset. However, we do not believe that resetting the interest accretion rates in a manner that recognizes any changes in estimated interest crediting and related expected cash flows on a level-yield basis over the remaining life of the contract would accurately reflect the amounts credited to a policyholder that are dependent on asset returns. Contracts with discretionary participation features are spread-based products; therefore, we believe it is useful to financial statement users to have transparency into an amount presented as interest expense that is representative of the amount credited to policyholders in the period, as opposed to a calculated amount that presents interest expense utilizing a level-yield approach. Application of the proposed level-yield method will not reflect the true economics and spread-based strategy of the insurance contract, as amounts reflected within interest expense will not be reflective of the actual credited amounts, thus distorting net income and misleading financial statement users.

Consistent with other areas within the Proposed ASU that apply a principles-based approach, we believe the method to reset the interest accretion rate for insurance contracts with discretionary participation features should also be principles-based. We propose the interest accretion rate should be reset in a manner reflective of the amounts expected to be credited to the policyholder within each reporting period. We believe this principles-based approach will help meet the Board's objective of presenting interest expense consistent with the variable rate nature of how these liabilities are financed through asset returns.

Margin for Contracts Measured Using the Building Block Approach

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

Yes. With the exception of reinsurance gains where the loss on the underlying direct contracts has already been recognized, which is discussed further in our response to question 36, we agree that an insurer should not recognize a gain at initial recognition of an insurance contract, but rather defer that amount as profit to be recognized in the future as the performance obligation is fulfilled. In addition, as discussed in question 13, we support that the margin should be adjusted for changes in future estimated cash flows to maintain and provide consistent application of this principle throughout the life of an insurance contract. We believe the guidance within the Proposed ASU to "lock" the margin at initial recognition and recognize subsequent changes in estimated cash flows immediately in net income introduces inconsistency. For example, favorable changes in future estimated cash flows would result in immediate gains to be recognized within net income, which is inconsistent with the Proposed ASU, which prohibits the recording of gains at initial recognition of an insurance contract.

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

We do not believe a comprehensive reconsideration of the current accounting framework for insurance contracts is necessary if full convergence will not be achieved. As this is a key area of divergence, if the Board decides to proceed with the Proposed ASU, we support the Board's single margin approach. While we understand the theory behind a risk adjustment, we have concerns that the costs of a dual margin approach outweigh these benefits. The acceptance of risk to earn a profit represents the underlying economics of an insurance contract. As the explicit risk adjustment and contractual service margin both represent deferred profit for acceptance of this risk at inception of the contract, we believe it would be arbitrary and complex to divide this deferred profit into multiple components. In addition, we are concerned the techniques used to estimate a risk adjustment are far too subjective, may introduce bias and would result in inconsistency between insurers' financial results. The Board's single margin would eliminate the need to use subjective methods that decrease comparability as it is calibrated to inflows and outflows at inception of a contract.

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

Not applicable. As previously discussed in our response to question 22, we support the Board's margin approach. However, for those reasons discussed in questions 13, we support the IASB's decision to unlock the margin for changes in estimated future cash flows; however, we support unlocking of the margin to allow for adjustment of the margin as if the change in estimated cash flows was known at inception of the insurance contract. See Exhibit 1 for further details.

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

Partially. Consistent with general loss criteria within current U.S. GAAP, we agree that expected losses should be recognized immediately. However, we believe that these expected losses should be based upon the actual economic nature of the insurance contract, and not an expected loss that results as a function of the BBA. For example, we have concerns regarding potential loss recognition for certain spread-based annuity products (e.g., single premium immediate annuity) that will be within scope of the Proposed ASU. For those products, we have concerns that the BBA would preclude the inclusion of all expected investment earnings within the fulfillment cash inflows, as the discount rate determined in accordance with the Proposed ASU is not representative of an expected net earned rate (i.e., a pricing rate). As a result, spread-based annuity products, whose underlying profitability is highly dependent upon the investment earnings and interest credited to the policyholder, may result in an expected loss that is solely a function of the BBA, and does not indicate the actual underlying profitability of the contract. We recommend that the Board further consider those insurance contracts that will be measured under the BBA that may not include all the respective revenue streams that are integral to the economics of the insurance contracts. We believe that a final standard that results in the recognition of expected losses due to a function of the measurement model is inappropriate and will mislead financial statement users.

As previously discussed, we do not agree that an entity should discount the reserves (i.e., the liability for remaining coverage and liability for incurred claims) calculated under the PAA. Therefore, when facts and circumstances indicate that a portfolio of contracts may be onerous, we believe that the onerous contract test should be performed on an undiscounted basis, with the option to include expected investment income. This

approach is consistent with current U.S. GAAP and considers a revenue stream that is integral in determining the pricing and profitability of an insurance contract. Therefore, exclusion of investment income when performing an onerous contract test may result in the recognition of expected losses for insurance contracts that are actually profitable, leading to confusion and information that is not useful to financial statement users.

If the Board decides to retain the requirement to discount the liability for remaining coverage and liability for incurred claims, we continue to have concerns about ignoring the impact of expected investment income in the onerous contracts test. We acknowledge that discounting the fulfillment cash flows already contains some impact of expected investment income. However, we believe that the proposed methods of determining the discount rate of the liability, as required by the Proposed ASU, do not capture the complete effect of expected investment income. Due to the importance of expected investment income in determining the profitability of an insurance contract, we believe that the requirement to exclude investment income would need to be reconsidered if the Board retains the discounting requirements.

In addition, we do not agree with the inclusion of potential catastrophic events in an onerous contract test, as portrayed in Example 13 of the Board's Proposed ASU. The uncertain nature of a catastrophic event's occurrence, severity and timing are factors that we believe make it imprudent for a company to forecast and record an expected loss when the catastrophic event has not yet occurred. In addition, recording an expected loss for such a significant and uncertain event before it has occurred, adversely affected the policyholder, or before the loss could be practically estimated would not provide a faithful representation of an insurance contract's liability and is inconsistent with the "incurred loss" PAA model.

Example 13 of the Board's Proposed ASU requires establishment of an onerous contract loss for an expected catastrophic event, even if the catastrophic event does not occur. As a result, the onerous contract loss reserve would remain, with disclosure of updated assumptions and the status of the catastrophic event. We do not believe that having a significant loss recorded for an event that has not occurred as of the reporting period would provide a faithful representation of the insurance liability. Such a practice would lead to confusion and mislead financial statement users.

To illustrate how recognizing a loss due to a potential catastrophic event may impact our financial statements, we have provided an example based upon recent events. In late August 2011, there was an indication of a tropical storm occurring in the Atlantic. On August 30th, the National Oceanic and Atmospheric Administration forecasted this tropical storm would become a major hurricane ("Hurricane Katia") within the week. Based upon Hurricane Katia's prediction path, the southeast United States was at risk. At the end of August, models would have predicted that a category 3-4 hurricane hitting the Carolinas would result in a significant level of expected losses to Nationwide. Subsequent to August month end, it had become known that Hurricane Katia never made landfall in the United States. Therefore, if August were a reporting period, we believe that recording a material expected loss for Hurricane Katia, prior to it actually being incurred, would have significantly misrepresented Nationwide's insurance contract liabilities and financial performance, thus misleading financial statement users.

In addition to the concerns discussed above, we believe that current U.S. GAAP within ASC 855 (Subsequent Events) provides adequate guidance for the accounting and reporting of (1) additional information obtained or (2) significant events occurring subsequent to the reporting date. ASC 855-10-55-2 provides a specific example for a natural disaster (e.g., a hurricane) that occurs after the reporting date. ASC 855 (Subsequent Events) provides that a natural disaster occurring subsequent to a reporting date would not be recorded within the financial statements, but included as a disclosure (i.e., nonrecognized subsequent event). To alleviate the identified concerns within Example 13 of the Board's Proposed ASU discussed above, we propose that the Board maintains the practice within current U.S. GAAP, which requires losses to be recorded for catastrophic events only when the event has occurred, the event adversely affects the policyholder, and the loss can be reasonably estimated. Catastrophic events occurring after the reporting date will continue to be adequately accounted and reported for under ASC 855 (Subsequent Events).

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

Yes. We support a principles-based approach that recognizes that the margin as an entity is released from risk under the insurance contract.

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

Yes. As the margin represents the present value of expected profits at inception of the contract, we agree interest should be accreted on the margin to reflect the time value of money and subsequently amortized into insurance contract revenue. As noted within question 13, we view the margin as the expected profit of a portfolio of insurance contracts and we support the IASB's approach to unlock and measure the margin consistently over the life of the insurance contract to provide a faithful and current representation of the expected profitability that will be recognized. Therefore, we propose the interest accretion rate on the margin should be updated each reporting period to provide consistency in measurement of the margin and the measurement of the fulfillment cash flows component of the insurance contract liability. In addition, utilizing an updated interest accretion rate will provide a current measurement of the expected profit of a contract, which we believe is useful information to financial statement users and a more faithful representation of the expected profit of the portfolio of insurance contracts.

Examples within the Proposed ASU tend to ignore accretion of interest for simplicity. However, we believe it is important to illustrate the mechanics of how the time value of money may impact the insurance contract liability, interest expense and insurance contract revenue. Therefore, we believe if the Proposed ASU is adopted, a final standard should include additional clarity and detailed examples that are not overly simplistic to illustrate the mechanics of accruing interest on the margin, as well as the subsequent amortization into insurance contract revenue.

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

No. We do not believe the remaining margin should be recognized immediately in net income when the expected cash outflows (including qualifying acquisition costs) of a portfolio of insurance contracts will exceed expected cash inflows. We believe the immediate recognition of a gain in periods in which assumptions change, such that a portfolio is expected to generate a loss, will result in counter-intuitive financial results that are not useful to financial statement users and are not representative of an insurance company's business. In addition, we believe it is inconsistent to require adjustment of the margin for losses when a portfolio of insurance contracts is expected to generate a loss, and to not require adjustment of the margin when there are changes in estimated cash flow assumptions that impact the portfolio of contracts expected profitability. For the reasons discussed in question 13, we support the approach to adjust the margin for changes in estimated future cash flows of an insurance contract with retrospective application. We believe adjusting the margin for current estimated future cash flows would eliminate the requirement of an onerous contract test for long duration contracts, which may result in the recording of immediate gains and counterintuitive financial results as discussed above.

Acquisition Costs

Question 28: Do you agree that the direct acquisition costs presented with the margin should include only the costs directly related to the entity's selling efforts that result in obtaining the contracts in the portfolio and that all

other acquisition costs should be recognized as expenses when incurred? If not, what do you recommend and why?

No. We believe the accounting guidance for direct acquisition costs is a fundamental area within the Proposed ASU that should be converged between the Board and the IASB. We support the IASB's approach, which requires the inclusion of direct acquisition costs, including those acquisition costs incurred that are attributable to unsuccessful efforts, within fulfillment cash flows of the insurance contract liability measurement. We believe all direct acquisition costs, including those related to unsuccessful efforts, are costs that arise directly from an insurance contract or can be attributed to them on a reasonable and consistent basis and are factored into the determination of an insurance contract's expected profitability. Therefore, to meet the Proposed ASU's key objective to provide decision-useful information that faithfully represents an insurance company's liabilities, we believe the inclusion of these direct acquisition costs within fulfillment cash flows is necessary to provide a faithful representation of an insurance contract's expected profitability.

Furthermore, although during the adoption of ASU 2010-26, Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts, the final consensus from audit firms with regards to wholesaler distribution models was that the bulk of the activities they performed were not direct enough to qualify as direct acquisition costs, we continue to believe the proposed guidance results in economically similar acquisition costs (e.g., commissions) receiving different accounting treatment, depending on whether the person performing the acquisition activity is an independent third party or an employee. Therefore, we respectfully request the definition of "direct" as used in the Proposed ASU section 834-10-55-104 be clarified so as to provide that the sales force contract selling activities performed by a wholesaler in order to facilitate another party selling the contract qualifies as direct, even though the wholesaler may not actually interact with the customer themselves. This would eliminate the issue with having different distribution models ending up with different accounting treatment for economically similar activities.

As discussed throughout the comment letter and Appendix, if full convergence can not be reached between the Board and the IASB on key issues such as the accounting for direct acquisition costs, we do not believe the Proposed ASU has met one of its key objectives, which is to provide comparability amongst companies (e.g., U.S. and International insurance companies). Without full convergence, we do not believe the Proposed ASU represents an improvement to current U.S. GAAP, given the significant amount of incremental and ongoing costs for preparers to implement such a comprehensive change to current U.S. GAAP, as well as the subsequent downstream economic impact to policyholders, investors, analysts and other financial statement users.

Finally, when ASU 2010-26 was issued, it contained a provision that stated "if the initial application of the amendments in this Update results in the capitalization of acquisition costs that had not been capitalized previously by an entity, the entity may elect not to capitalize those types of costs." As this guidance is not proposing any significant changes to the items that can be capitalized, we believe that a similar provision should be considered and included within the Proposed ASU relating to acquisition costs. We believe that this will help minimize the costs of adopting the Proposed ASU.

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

No. As discussed in questions 10 and 28, we support the IASB's approach, which requires the inclusion of direct acquisition costs, including those acquisition costs incurred that are attributable to unsuccessful efforts, within the fulfillment cash flows of the insurance contract liability measurement for contracts measured using the BBA. We believe inclusion of these direct acquisition costs within the fulfillment cash flows will provide (1) consistency with the treatment of other fulfillment cash flows, and (2) a faithful representation of the expected profitability of the insurance contracts.

For insurance contracts measured using the PAA, we believe direct acquisition costs should be capitalized and presented separately on the balance sheet as an asset. The Board has indicated it views the PAA as a separate model from the BBA, and the PAA is essentially modeled after the proposed revenue recognition standard. Under the proposed revenue recognition standard, deferred acquisition costs are capitalized as an asset and amortized into income over the life of the performance obligation. Similarly, we believe the direct acquisition costs for insurance contracts accounted for under the PAA should apply a consistent concept of capitalization and reporting as the proposed revenue recognition standard. Although this will create a difference between insurance contracts measured using the PAA and those measured using the BBA, it will create consistency for insurance contracts measured using the PAA and contracts under the proposed revenue recognition standard. Further, we believe the difference created between insurance contracts measured using the PAA and those measured using the BBA is supportable, given that these approaches currently have separate and distinct models under the Proposed ASU.

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

No. As discussed within our responses to questions 10, 28, and 29, we support the IASB's approach that requires the inclusion of direct acquisition costs, including those acquisition costs incurred that are attributable to unsuccessful efforts, within fulfillment cash flows of the insurance contract liability measurement for contracts measured using the BBA. Consistent with the treatment of other fulfillment cash flows, we believe direct acquisition costs should be recognized as an expense in net income when actually incurred, with a corresponding release of the insurance contract liability into revenue for the expected direct acquisition costs to be incurred in that period.

We agree that for contracts measured using the PAA, acquisition costs should be recognized as an expense in net income in the same pattern that it recognizes the liability for remaining coverage.

Insurance Contract Revenue

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

No. We do not believe insurance contract revenue, as it is defined within the Proposed ASU, is a faithful representation of the economics of an insurance company. Further, we do not believe it will provide relevant and decision-useful information to financial statement users. The earned premium model to present insurance contract revenue is materially different from what financial statement users are accustomed to for insurance companies that issue life insurance or other long-term insurance contracts and will fundamentally change how these financial statements should be understood. As a result, significant education efforts will be needed to help management, boards of insurance enterprises, analysts, ratings agencies and other key financial statement users to understand this new basis of accounting. Our belief is that even with these educational efforts to help users understand the new measurement model and financial statement presentation, the information provided within the financial statements would not result in an improvement in decision-useful information over current U.S. GAAP; rather, the presentation requirements will result in the obscurity of information and increase confusion in understanding insurance company financial statements. Further, management will have to maintain an additional set of financial records that will serve as a managed reporting view, which will be significantly different from the

U.S. GAAP financials, as the Proposed ASU will not provide decision-useful information for the company or financial statement users.

The fundamental measurement of an insurance contract liability under the BBA is based upon an expected cash flow model; however, the presentation requirements under the Proposed ASU do not provide an understanding of those cash flows and do not reflect the underlying nature and economics of the company's insurance contracts. As a result, decision-useful information about the underlying nature and economics of the company's insurance contracts are not reflected within the financial statements and users will not have the relevant information to understand and make economic decisions based upon a presentation approach that does not reflect the underlying measurement model of insurance contracts under the Proposed ASU. We believe the result of providing information that is not useful to financial statement users will result in an increased use of non-GAAP measures to obtain the necessary information that has been historically utilized to evaluate and analyze insurance companies. In addition, this fundamental change to current U.S. GAAP will result in significant incremental and ongoing costs as discussed in our response to question 47, which will have a downstream economic impact to preparers, policyholders, investors and other financial statement users.

We acknowledge that the theoretical merit of the earned premium approach is based upon the principles of revenue recognition within current U.S. GAAP; however, we believe the life insurance industry is different due to the long-term nature of its insurance contracts. The very nature of insurance contracts is the reason the Board has proposed separate accounting guidance from other revenue recognition principles. It is because of this difference that the concept of an "earned premium" has not historically been a relevant measure that would be the focus of management, investors, analysts and other financial statement users.

If the Board continues to proceed to comprehensively change current U.S. GAAP, we believe that it is imperative that an alternative comprehensive presentation approach be developed that does not change how insurance company financial statements are understood and more importantly that provides relevant and useful information that has the unanimous support of investors, analysts, management, preparers, and other financial statement users. We believe adopting a standard that does not provide decision-useful information to financial statement users will result in significant incremental and ongoing costs, with little benefit over current U.S. GAAP.

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

No. We believe that the Proposed ASU's requirement to exclude "estimated returnable amounts" (i.e., any amounts received that an entity is obligated to pay to policyholders or their beneficiaries regardless of whether an insured event occurs) will introduce significant operational complexity and subjectivity in estimating these amounts each reporting period, which will result in divergence of industry practice and a lack of comparability. In addition, companies will incur significant incremental costs for enhanced processes and controls around updating these assumptions and determining the estimated returnable amounts each reporting period, with little added benefit over current U.S. GAAP requirements. Therefore, we support guidance which requires that premiums allocated to a policyholder's explicit account balance within universal life-type contracts, deferred annuities and variable and equity-based life and annuity products be excluded from revenue and that any subsequent return of the account balance is not recognized as an expense. Currently, explicit account balances are tracked by insurers and there is little to no subjectivity in identifying the amount of the account balance or the premium (and benefits) to be excluded from the Statement of Comprehensive Income.

Question 33: For contracts measured using the premium allocation approach, do you agree that if the contract has a financing component that is significant to the contract, an entity should adjust the liability for remaining coverage to reflect the time value of money and recognize the accretion of interest with insurance revenue? Do

you agree with the practical expedient that an entity should not be required to reflect the time value of money in measuring the liability for remaining coverage (that is, if the entity expects, at contract inception, that the time period between when the policyholder pays all or substantially all of the premium and when the entity provides the corresponding part of the coverage is one year or less)? If not, what do you recommend and why?

No. Consistent with our response for discounting of the liability for incurred claims in question 15, we do not believe it will result in decision-useful information for financial statement users.

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

Yes. We believe sufficient guidance on how to determine insurance contract revenue is provided within the Proposed ASU. However, as discussed within the comment letter and other questions within the Appendix, we do not support the presentation of insurance contract revenue, as it is determined under the Proposed ASU, as it is fundamentally different from the decision-useful information utilized by management and expected by financial statement users. Therefore, this will result in the increased usage of non-GAAP measures to analyze an insurance company.

Participating Contracts

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

Yes. We believe participation features that are contractually dependent on the performance of other assets or liabilities of the insurer, or the performance of the entity itself, should be measured on the same basis used to measure the underlying items and changes in the measurement should be presented in the same statement. We also agree this approach should be limited to participating features for which the amount of the performance of the underlying items passed through to policyholders is contractually determined.

Reinsurance

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

No. In general, we agree with the accounting for reinsurance contracts under the Proposed ASU; however, the recognition of reinsurance should be consistent with the underlying contracts. Specifically, we believe gains should be recognized based on the terms of the reinsurance agreement (e.g., proportional) to the extent losses on the underlying contracts have been recognized.

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

Yes.

Insurance Contracts Acquired in a Business Combination

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

No. We do not agree that entities should record an immediate loss at acquisition. In most business combinations, if the purchase price cannot be allocated to identifiable assets and liabilities, whether tangible or intangible, any positive balance is recognized as goodwill. As such, we believe this proposed guidance to recognize an immediate loss is counterintuitive to any other business combination and we do not believe that it represents the economics of the transactions. As fair value is determined using non-performance risk and the value of expected future profits embedded in the pricing of the insurance contracts acquired, we believe that inherently the fair value of the insurance contracts will usually be less than the insurance contracts measured in accordance with the Proposed ASU, which will result in an immediate loss for most business combinations. As businesses are acquired with future growth and profit in mind, we believe this is a significant issue for most insurance entities and sends the wrong message to investors. Under current business combination guidance, we would establish an identifiable intangible asset that represents the value of the business acquired, which would be amortized based on the life of the contracts acquired in conjunction with the business combination. We believe this approach is more appropriate because it acknowledges the future profits of the business acquired, and does not send a counterintuitive message to the financial statement users that a loss was incurred by purchasing an entity. Likewise, since portfolio transfers are economically similar to business combinations, we believe that the accounting should also be consistent.

We agree entities should record a margin (not an immediate gain) for the amount that the fair value of the asset and liability balances exceeds those assets and liabilities, measured in accordance with the guidance in this Proposed ASU. We believe this produces a result that is consistent with other positions within the Proposed ASU.

Contract Modifications

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

No. We believe the Proposed ASU has inadvertently made the contract modification guidance overly complex and not useful. Our belief is that our recommendations within the comment letter and Appendix will eliminate the need to assess insurance contracts for modification if it is accounted for under the BBA.

The accounting requirements for insurance contract modifications is based upon the premise of how to account for deferred acquisition costs when an insurance contract's benefits, features, rights or coverages have been modified. As discussed within the response to question 30, we believe direct acquisition costs for those contracts under the BBA are costs that arise directly from an insurance contract or can be attributed to them on a reasonable and consistent basis and are factored into the determination of an insurance contract's expected profitability. Therefore, we believe that direct acquisition costs should not be specifically capitalized as a component of the margin when incurred, but rather included within fulfillment cash flows of the insurance contract liability measurement and treated similarly as all other fulfillment cash flows (i.e., recognized as an expense in net income when actually incurred, with a corresponding release of the insurance contract liability into revenue for the expected direct acquisition costs to be incurred in that period). As our recommendation would treat direct acquisition costs similarly to all other fulfillment cash flows and result in the recognition of an expense in net income when the costs are incurred, we do not believe specific contract modification guidance to account for treatment of direct acquisition costs would provide any benefit.

Based upon the Proposed ASU, the assessment of whether a contract has been modified (whether substantially or non-substantially) would have a resulting impact on the margin recognized on the Statement of Financial Position, as well as potential gain/loss recognition within the Statement of Comprehensive Income. We believe that a modified contract is a continuation of the original contract and represents updated cash flow assumptions. As discussed in the comment letter and our response to question 13, we recommend the margin for contracts measured under the BBA be unlocked for changes in future estimated cash flows. As a result, we believe unlocking the margin would simplify the accounting requirements for contract modifications as all changes in estimated fulfillment cash flows for substantial and non-substantial contract modifications would be accounted for as adjustments to the margin.

Based on the above, our recommendations would simplify and eliminate the need to assess insurance contracts for modification if accounted for under the BBA. As such, we believe that this section of the Proposed ASU should be eliminated.

If the Board proceeds to require the locking of the margin, then we believe the contract modification guidance within the Proposed ASU requires additional clarification. In the Board's attempt to carry over the contract modification guidance from ASC 944 (Financial Services – Insurance), we believe important aspects of this guidance were not addressed. For example, paragraph 834-10-40-4 provides that a contract modification occurs “when the parties to the contract approve a change in the terms of a contract.” However, current contract modification guidance within ASC 944 (Financial Services – Insurance) indicates that contract modifications could result from the election by the contract holder of a benefit, feature, right or coverage that was within the original contract. Due to the change in the definition of a contract modification, we believe it is important to further clarify the new definition to avoid confusion and diversity in practice. Consistent with ASC 944 (Financial Services – Insurance), we would recommend providing examples that illustrate when a contract modification may or may not occur.

If an insurance contract is accounted for under the PAA, we believe that the proposed modification guidance is appropriate. We believe that the difference between contracts accounted for under the PAA versus the BBA is supported by the separate accounting model concept.

Presentation

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

No. As discussed throughout the comment letter, we have significant concerns with the overall presentation requirements for insurance companies that issue life insurance or other long-term insurance contracts and we believe this approach will not result in an improvement in decision-useful information over current U.S. GAAP; rather, the presentation requirements will result in the obscurity of the financial statements, leading to increased usage of non-GAAP measures. The fundamental measurement of an insurance liability under the BBA is based upon an expected cash flow model. Therefore, we believe it is important that information presented within the financial statements provide an understanding of those cash flows, in order to understand the nature and economics of the company's insurance contracts. As discussed within our response in question 31, we have specific concern with regards to the earned premium approach to present insurance contract revenue.

In addition, we do not support the presentation requirements for segregated fund arrangements. The Proposed ASU's requirement to present investment income on segregated fund accounts within the Statement of Comprehensive Income, separately from the interest expense representing the pass-through of that investment income, will lead to confusion for users of the financial statement. This will result in misleading yields on an insurance company's assets that will not faithfully represent the investment performance of an insurance company. We believe that the current U.S. GAAP requirement to offset investment performance and the corresponding amounts credited to a contract holder would provide the most meaningful presentation to the financial statement users, as it allows users to readily analyze investment returns of an insurance company by excluding amounts earned on segregated fund assets that are fully passed through to policyholders and therefore not available to shareholders.

We believe the requirement to present investment income and the related pass-through is conceptually inconsistent with the asset management industry, which only requires the presentation of the fees earned and not the resulting investment income on assets managed and subsequent pass-through, and with accounting principles for a principal-agent relationship within the revenue recognition accounting literature. We believe that the nature and economics of segregated fund arrangements currently within the insurance industry should be retained.

In addition, we believe that companies should have the option to present the liability for segregated fund arrangements within the insurance contract liability, or separately, on the Statement of Financial Position. Presenting segregated fund arrangements and the assets that support them separately from other items on the Statement of Financial Position better reflects the true risk to the insurance company.

As discussed above, we believe the presentation requirements within the Proposed ASU do not provide an improvement in decision-useful information over current U.S. GAAP and will provide little relevance to financial statement users. In addition, the presentation requirements will result in counterintuitive information that will obscure the true nature and economics of insurance contracts, provide misleading financial results and lead to confusion in the understanding of an insurance company's financial statements and increased usage of non-GAAP measures. If the Board continues to proceed to comprehensively change current U.S. GAAP, we believe that it is imperative that an alternative comprehensive presentation approach be developed that does not change how insurance company financial statements are understood and more importantly that provides relevant and useful information that has the unanimous support of investors, analysts, management, preparers, and other financial statement users.

Disclosure

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

No. We do not agree that the exorbitant amount of disclosures will help the financial statement users better understand the financial position of the company, and we question the highly prescriptive nature of some of the requirements. We believe the amount of information in its entirety will overwhelm users with insignificant details and distract them from meaningful points of analysis. The amount of the disclosures will lead to a large disparity in the disclosure requirements between companies. Also, companies will have a hard time compiling this information by required deadlines, whether internal or external, due to the extensive nature of the requirements.

Further, we believe the disclosure requirements should be limited for nonpublic entities. Given that the financial statement users are generally more limited in these entities, the disclosures requirements should consider this fact.

As the disclosures become more complex and voluminous, we have serious concerns relating to confidential or proprietary information being disclosed. We believe several of the disclosures require information that represents a competitive advantage to companies and that by disclosing it, others will be able to benefit. Due to this, we believe companies will either make their disclosures so limited that they are not useful or disclose so much that they will be negatively impacted with others benefiting. Specifically, our concerns relating to the confidential or proprietary information are centered on the disclosure requirements contained in the Proposed ASU in sections 834-10-50-24, 834-10-50-25, 834-10-50-29 and 834-10-50-3.

Finally, with the exception of our alternative approach to discounting PAA reserves discussed in question 15, we disagree with the Proposed ASU's requirement that sensitivity analysis should be disclosed in the financial statements. We believe the sensitivity analysis creates information that can be misapplied and misunderstood. Specifically, our concerns are focused on the disclosure requirements contained in the Proposed ASU sections 834-10-50-31 and 834-10-50-34. If the Board decides to retain these disclosures, we suggest that all sensitivity analysis should be in narrative form and at a high enough level where the information will be useful to and easily understood by the financial statement users. We believe the level should be consistent with the measurement approach (i.e., group all insurance contracts accounted for under the PAA and group all insurance contracts accounted for BBA).

Based on the above, we believe the Board should revisit the disclosure requirements of the Proposed ASU and determine which disclosures are really necessary, meaningful and useful to the financial statement users. We believe this should be accomplished through extensive outreach to the investor and analyst community. Further, we believe these reconsiderations should consider the inappropriate disclosure of confidential and proprietary information.

Effective Date and Transition

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

The most significant drivers affecting the implementation of the Proposed ASU include: current system constraints, historical information constraints and the development of processes and controls. Current systems are not equipped to handle the requirements of the Proposed ASU. Updating systems will require significant system modifications, and in many situations, development of new systems entirely. Historical information is maintained by most entities; however, the amount of historical information that is needed and maintained varies by entity. To implement the Proposed ASU accurately, the historical information will have to be accumulated, developed and reviewed. Also, public companies have filings with the Securities and Exchange Commission that include a five year financial information disclosure, which causes increased information needs and further complexities. Finally, as the Proposed ASU represents significant and fundamental changes to the insurance industry, new processes and controls will need to be developed, operationalized and monitored upon adoption

and on a go-forward basis. Based on the above, we believe that the effective date of the Proposed ASU should not be earlier than six years after the issuance of the Proposed ASU. While we realize six years may seem to some as an unnecessarily long window for implementation, when compared with the typical two to three year window provided for other convergence projects, which are far less complex and represent far less of a comprehensive change as the Proposed ASU, we believe six years to be both a reasonable and necessary window.

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

No. We generally agree that the effective date of proposed guidance should be different for public and nonpublic entities. However, Nationwide has several public entities that are consolidated by nonpublic entities. In these cases, we believe companies should have the ability to adopt the Proposed ASU for the nonpublic entities, at the same time it is effective for the public entities. This will allow for consistency of application, stream-lined reporting and implementation activities and less confusion for financial statement users of both sets of financial statements.

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

No. We appreciate the Board's efforts to make the transition guidance of the Proposed ASU as operational as possible with the use of practical expedients (e.g., determining of portfolios at transition). However, given the operational challenges in determining the margin at transition, even utilizing the practical expedients provided, we strongly encourage the Board to consider allowing preparers the option to use the practical expedient provided in the proposed IASB standard, as outlined in paragraphs C5 and C6, which allows the ability to use the benefit of hindsight in determining the cash flows necessary to determine the margin at the transition date. We believe that using hindsight to consider what has actually occurred at transition would not only alleviate significant operational burdens for preparers to gather historical assumptions, but would also greatly improve both verifiability and comparability, while still providing a margin at transition that faithfully represents the profit remaining for the contracts in force upon transition.

While we understand there may be conceptual concerns with using hindsight for determining the margin at transition, as it is the equivalent of having "unlocked" the margin between inception and the transition date, we believe that such treatment is warranted in these circumstances. We believe a margin calculated in this way provides a more relevant measure to financial statement users than defaulting to a zero margin if the necessary information is unavailable, while providing potentially significant cost savings related to the transition portion of the guidance.

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

No. Due to lack of historical information and the timing of certain business combinations, it may be difficult, if not impossible, to reallocate the fair value of the asset and liability balances related to insurance contracts in a business combination that occurred prior to the transition date. As such, we believe a practical expedient should be developed to ease this burden.

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

No. We appreciate the Board's efforts to make the transition guidance of the Proposed ASU as operational as possible. If the Board agrees with our proposed recommendation included in question 44, we believe that the financial statement users will be provided with relevant information that appropriately balances comparability with verifiability.

Costs and Complexities

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

The most significant drivers affecting the incremental costs of implementing the Proposed ASU include current system constraints, historical information constraints and development of processes and controls. Current systems are not equipped to handle the Proposed ASU. Updating administration, claims, actuarial and reporting systems to account for the Proposed ASU will require significant system modifications, and in many situations, development of entirely new systems. With the new systems comes the additional cost of training. Historical information is maintained by most entities; however, the amount of historical information that is needed and maintained varies by entity. To implement the Proposed ASU accurately, the historical information will have to be accumulated, developed and reviewed. Finally, as the Proposed ASU represents significant and wholesale changes to the insurance industry, new processes and controls will need to be developed and established upon adoption. For example, we would expect to incur significant additional costs for enhancing processes and controls around the updating of assumptions each period, several of which are new assumptions not previously required to be determined (e.g., determination of "estimated returnable amounts," amount of insurance contract revenue recognition each period for contracts measured using the BBA, discounting for contracts measured using the PAA, etc.).

The most significant drivers affecting the ongoing costs of the Proposed ASU include explanation of financial results, operating and monitoring processes and controls, additional analysis caused by the significantly changed definition of a portfolio, additional complexities in actuarial estimates and development of financial statements and disclosures. Significant resources will need to be expended on a regular basis to ensure analysts and financial statement users understand the true risks and financial position of the company. Further, management will have to maintain an additional set of records that will serve as a managed reporting view, as the Proposed ASU does not result in decision-useful information for the company or financial statement users. In addition, from all of the processes and controls that are established upon adoption, continuous resources will be needed to ensure they are operating and monitored on a go-forward basis. Due to increased complexity in the actuarial estimates, additional resources will need to be expended to comply with the Proposed ASU. Finally, given the significant volume of financial information that is required by the Proposed ASU within the financial statements and disclosures, significant effort and time will be expended to develop and continuously prepare the information.

Finally, the exorbitant costs associated with the adoption and continued application of the Proposed ASU may have negative effects on product pricing offered by insurers.

If the Board accepts the recommendations we have made, particularly with regard to the portfolio definition, the discount rate used to measure insurance contract liabilities, discounting of contracts measured using the PAA, unlocking of the margin, and the use of hindsight upon transition, we believe these will serve to reduce the costs of implementing and applying this Proposed ASU on an on-going basis.