IFRS – July 2013 Exposure Draft

Question 3

Do you agree that the financial statements would provide relevant information that faithfully represents the entity's financial performance if, for all insurance contracts, an entity presents, in profit or loss, insurance contract **revenue and expenses**, rather than information about the **changes** in the components of the insurance contracts

Why or why not ? If not, what would you recommend and why ?

Background

- 2010 ED proposed the format of the statement of comprehensive income (SCI) to take the form of a ***margin*** analysis and hence did not allow premiums to be reported but rather changes in components that make up the insurance liability*

- In effect, the summarised-margin approach would have treated all premiums as deposits and all claims and benefit payments as returns of deposits

- Information about premiums, claims and expenses would be provided only in the notes to the financial statements.

Summarised Margin model	**20XX**
Income statement	
Change in Risk adjustment	X
Change in Residual margin	X
Loss on initial recognition (if any)	X
Experience adjustment during the period(if any)	X
Change in estimates of cash flows (if any)	X
Unwind	X
Investment Income	X
Profit/Loss	**X**

* For contracts where the coverage is greater than 1 year

Background

2013 ED allows to show revenue and expenses in income statement;

- But **revenue** is formula driven, sum of:
  - Release of contractual service margin
  - Change in risk adjustment
  - Latest estimate of expected outgo
  - Premium portion covering acq: expenses

- Also, need to eliminate the deposit component of the premium that the insurer expects to pay regardless of whether an insured event occurs or not

- Ensures that the total insurance contract revenue over the duration of the contract is the same as the premiums received , adjusted for the time value of money.

Income statement	**20XX**
Insurance contract revenue	X
Actual Claims and benefits incurred	X
Amortisation of acquisition costs	X
Loss on initial recognition (if any)	X
Assumption changes (future) if any due to CSM being negative	X
Unwind	X
Investment Income	X
Profit/Loss	**X**

Question 3- Observations and Issues to consider

2013 ED proposes the concept of insurance contract revenue in response to the strong feedback received on the absence of ‘volume’ information as per the 2010 ED proposals. *Worth noting IASB considered the commonly used approaches currently (premium ‘written’ and ‘due’) before rejecting them on various grounds*

Will the ‘revenue’ measure that is formula driven and unrelated to ‘premiums collected’ acceptable to stakeholders?

Is the concept too complex to understand for users ?

Is the concept too complex to implement?

Question 3 - Observations and Issues to consider

On the current proposal to separate the deposit (investment component) from revenue and claims:

Is there enough clarity in the determination of investment component ?

Are there implementation challenges, where the current data and modelling systems might not capture the required information separately ?

Will separating the investment component, provide the necessary volume information as demanded by the community ?

Any other comments and observations please ?

Question 4

Do you agree that financial statements would provide relevant information that faithfully represents the entity's financial performance if, any entity is required to segregate the effects of the underwriting performance from the effect of the **changes in the discount rates** by:

a) Recognising, in profit or loss, the interest expense determined using the discount rates that applied at the date that the contract was **initially recognised**. For cash flows that are expected to vary directly with returns on underlying items, the entity shall update those discount rates when the entity expects any changes in those returns to affect the amount of those cash flows; and

b) Recognising, in other comprehensive income, the **difference** between:

   (i) the carrying amount of the insurance contract measured using the discount rates that applied at the **reporting date**; and

   (ii) the carrying amount of the insurance contract measured using the discount rates that applied at the date that the contract was **initially recognised**. For cash flows that are expected to vary directly with returns on underlying items, the entity shall update those discount rates when the entity expects any changes in those returns to affect the amount of those cash flows

Why or why not ? If not, what would you recommend and why ?

Background -1

- 2010 ED proposed that the effect of the changes in discount rates should always be presented in profit or loss.

- Hence, there was a criticism that the gains and losses from underwriting and investing activities would be obscured by more volatile gains and losses arising from changes in the current discount rate.

- At the same time, there was the comment that due to the market based measurement of liabilities and the option to account for most assets at fair value, the market related volatility (if any) will better reflect the real ALM risks.

Background -2

- 2013 ED proposes that an entity should recognise:

- In profit or loss interest expense determined on an amortised basis; and

- In ‘other comprehensive income’ the difference between the carrying amount of the insurance contract measured using the discount rates that were used to determine that interest expense , and the carrying amount of the insurance contract measured using the current discount rates.

- IASB was persuaded that entities should segregate the effects of changes in the discount rate so that users of financial statements could better assess the underwriting and investing performance of an entity.

- Like in other areas, here also IASB considered alternate views and rejected them based on various grounds.

Question 4 - Observations and Issues to consider

What is the proposed approach's impact on volatility - Reduce, Increase or Hide ?

Does the approach impact asset classifications under IFRS 9 ?

Should there be a choice given to the entity to take the discount rate change impact through OCI or income statement depending on their asset treatment ?

Implementation challenges ?
As the systems should now maintain a library of historical discount rates and the 'unwind' (taken through OCI) which is normally easy to explain will not be that easy !

Any other comments and observations please ?

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Thank You