1 November 2013

Mr Hans Hoogervorst
Chairman
International Accounting Standards Board
1st Floor 30 Cannon Street
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United Kingdom

(By online submission)

Dear Hans

RESPONSE TO REVISED EXPOSURE DRAFT ON INSURANCE CONTRACTS

The Singapore Accounting Standards Council (ASC), in conjunction with the Institute of Singapore Chartered Accountants (ISCA), appreciates the opportunity to comment on the revised Exposure Draft on Insurance Contracts (the 2013 ED) issued by the International Accounting Standards Board (the IASB) in June 2013.

General

We continue to strongly support the IASB's efforts to develop this much needed comprehensive standard for insurance contracts which would provide a consistent basis for the accounting for insurance contracts and eliminate accounting inconsistencies present in existing varied practices, and therefore improve comparability across entities, jurisdictions and capital markets. We appreciate the significant efforts made by the IASB to address constituents' concerns raised on the 2010 Exposure Draft on Insurance Contracts (the 2010 ED), including ours particularly on the measurement aspects of insurance contracts. We also applaud the IASB's efforts in increased outreaches to our constituents in the Asia-Oceania region.

Overall, we broadly agree with the 2013 ED proposals with the exception of the proposed treatment of changes in the estimates of the risk adjustment, and believe that the 2013 ED represents a significant improvement to the 2010 ED. Nevertheless, we are of the view that the principle-based requirements proposed in the 2013 ED would warrant additional application guidance in some areas in order to achieve the IASB's objective of enhanced comparability, notably on (a) the recognition of the contractual service margin (CSM) in profit or loss over the coverage period; and (b) the determination of a portfolio of insurance contracts.

Our comments on the specific questions in the 2013 ED are provided below. However, we would like to draw the IASB's attention to our proposals on the following areas:

I. Risk adjustment

We are of the view that changes in estimates of risk adjustment that are related to future coverage and other future services should be recognised in profit or loss over the coverage period on a systematic basis, rather than recognised immediately in profit or loss as proposed in the 2013 ED. We recommend that the IASB reconsider its position on this issue.

II. Mandatory effective date of IFRS 9 Financial Instruments and the proposed new Insurance Contracts standard

We believe that it is imperative that the IASB aligns the mandatory effective date of IFRS 9 to that of the proposed new Insurance Contracts standard so as to prevent accounting mismatches for insurers and to ensure that insurers would not have to face two rounds of major changes in a short period of time. Furthermore, a different mandatory effective date would add undue complexity for insurers in implementing the proposed new Insurance Contracts standard due to the need to re-designate financial instruments at transition. Accordingly, we urge the IASB to align the mandatory effective date of these two standards.

Question 1

Do you agree that financial statements would provide relevant information that faithfully represents the entity's financial position and performance if:

(a) differences between the current and previous estimates of the present value of future cash flows related to future coverage and other future services are added to, or deducted from, the contractual service margin, subject to the condition that the contractual service margin should not be negative; and

(b) differences between the current and previous estimates of the present value of future cash flows that do not relate to future coverage and other future services are recognised immediately in profit or loss?

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

We agree with the above proposal to account for differences between the current and previous estimates of the present value of future cash flows. In particular, we concur that the CSM represents the unearned profit in an insurance contract and as such, adjusting the CSM to reflect these changes in estimates of cash flows relating to future coverage and other future services (that affects future profitability of the insurance contract) would provide a more faithful representation of the remaining unearned profit in the insurance contract after inception.

We believe that the proposal to "unlock" the CSM would have a corresponding effect on the treatment of risk adjustments. As mentioned in the "General" section above, we disagree with the proposal to recognise changes in estimates of risk adjustment immediately in profit or loss. Rather, we consider that changes in estimates of risk adjustment that are related to future coverage and other future services should be recognised in profit or loss over the coverage period systematically. We recommend that the IASB reconsider its current position on this issue.

In addition, we are of the view that further clarity is required to illustrate the application of paragraph 32 of the 2013 ED on what constitutes a "systematic way that best reflects the remaining transfer of services that are provided under the contract". We believe that an illustrative example developed on this area would be useful.

Question 2

If a contract requires an entity to hold underlying items and specifies a link between the payments to the policyholder and the returns on those underlying items, do you agree that financial statements would provide relevant information that faithfully represents the entity's financial position and performance if the entity:

(a) measures the fulfilment cash flows that are expected to vary directly with returns on underlying items by reference to the carrying amount of the underlying items?

(b) measures the fulfilment cash flows that are not expected to vary directly with returns on underlying items, for example, fixed payments specified by the contract, options embedded in the insurance contract that are not separated and guarantees of minimum payments that are embedded in the contract and that are not separated, in accordance with the other requirements of the [draft] Standard (i.e. using the expected value of the full range of possible outcomes to measure insurance contracts and taking into account risk and the time value of money)?

(c) recognises changes in the fulfilment cash flows as follows:

- **(i) changes in the fulfilment cash flows that are expected to vary directly with returns on the underlying items would be recognised in profit or loss or other comprehensive income on the same basis as the recognition of changes in the value of those underlying items;**
- **(ii) changes in the fulfilment cash flows that are expected to vary indirectly with the returns on the underlying items would be recognised in profit or loss; and**
- **(iii) changes in the fulfilment cash flows that are not expected to vary with the returns on the underlying items, including those that are expected to vary with other factors (for example, with mortality rates) and those that are fixed (for example, fixed death benefits), would be recognised in profit or loss and in other comprehensive income in accordance with the general requirements of the [draft] Standard?**

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

We agree with the above proposal, which would create an exception to the general requirements of the 2013 ED, for contracts that require an entity to hold underlying items and specify a link between the payments to the policyholder and the returns on those underlying items. Specifically, this “mirroring approach” would eliminate any accounting mismatches when the terms of a contract mean that no economic mismatches would be suffered by the entity.

Question 3

Do you agree that 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 and why not? If not, what would you recommend and why?

We agree that the presentation of insurance contract revenue and expenses in the primary financial statements would provide relevant information that faithfully represents the entity’s financial performance, ensure consistent presentation for insurers that write short and long-tail businesses when different measurement models are used, and facilitate comparison of revenue across industries. In addition, we are of the view that the proposed presentation would enhance understandability to users of financial statements as the measures of activities undertaken by an entity would be based on commonly understood notions of revenue and expenses.

Moreover, we support the inclusion of the summarised margin information in the disclosure notes as we believe this piece of information would enhance users’ understanding of the sources of profit of an insurance entity.

Question 4

Do you agree that financial statements would provide relevant information that faithfully represents the entity’s financial performance if an entity is required to segregate the effects of the underwriting performance from the effects 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?

We agree that segregating the effects of changes in discount rate in other comprehensive income would enhance the reporting of an entity's underwriting performance.

Question 5

Do you agree that the proposed approach to transition appropriately balances comparability with verifiability?

Why or why not? If not, what do you suggest and why?

We agree with the proposed approach to transition as it would increase the comparability of insurance contracts in existence at the date of transition with those that are written after transition. In particular, we welcome the proposal to apply a modified retrospective approach at transition to reduce the difficulties inherent in a full retrospective approach.

Question 6

Considering the proposed Standard as a whole, do you think that the costs of complying with the proposed requirements are justified by the benefits that the information will provide? How are those costs and benefits affected by the proposals in Questions 1–5?

How do the costs and benefits compare with any alternative approach that you propose and with the proposals in the 2010 Exposure Draft?

Please describe the likely effect of the proposed Standard as a whole on:

(a) the transparency in the financial statements of the effects of insurance contracts and the comparability between financial statements of different entities that issue insurance contracts; and

(b) the compliance costs for preparers and the costs for users of financial statements to understand the information produced, both on initial application and on an ongoing basis.

On balance, we believe that the costs of complying with the proposed requirements are justified by the benefits that the information will provide.

Nonetheless, the costs of complying with the proposed requirements should not be underestimated. We foresee that entities would need to put in place new systems and processes to implement the proposed requirements as current systems are unlikely to have been designed to allow the information required under the proposed requirements to be readily extracted and used. Moreover, there would be additional modelling efforts required to measure insurance contract liabilities and to split them into the various components in accordance with the proposed requirements.

In addition, the proposed presentation requirements would be operationally complex for entities to implement as items required to be presented in the financial statements would need to be derived from sources other than the chart of accounts. This may entail significant changes to the existing information technology systems in order to meet the proposed presentation requirements.

As such, we believe that the IASB must ensure a minimum lead time of three years for entities to implement the proposed requirements.

Question 7

Do you agree that the proposals are drafted clearly and reflect the decisions made by the IASB?

If not, please describe any proposal that is not clear. How would you clarify it?

In addition to our comments to the preceding questions, we believe that there is merit for the IASB to provide clarification and further guidance in the following areas:

- The 2013 ED defines a portfolio of insurance contracts as "a group of insurance contracts that provide coverage for similar risks and are priced similarly relative to the risk taken on; and are managed together as a single pool". However, it does not contain any guidance on how a portfolio of insurance contracts should be determined. For example, it is unclear whether new insurance contracts that otherwise have similar insurance features as an existing portfolio of insurance contracts but which are priced differently due to experience adjustments should be included within the portfolio. We recommend that the IASB provide further guidance on how a portfolio of insurance contracts should be determined as this has significant implications on the accounting for insurance contracts.

- The 2013 ED does not contain any guidance on how derecognised insurance contracts should be reflected in profit or loss, particularly in relation to the CSM and risk adjustments associated with lapsed and/or expired insurance contracts, and whether they should be separately presented in profit or loss. Further guidance in this would be useful.

Other Comments

<u>Align the mandatory effective date of IFRS 9 to that for the proposed new Insurance Contracts standard</u>

As mentioned in the "General" section above, we believe that it is imperative that the IASB aligns the mandatory effective date of IFRS 9 to that for the proposed new Insurance Contracts standard and we had, on numerous occasions urged the IASB to do so. Taking into account the complexities of implementing the proposed new Insurance Contracts standard and the complexities of implementing a 2-step implementation (IFRS 9 followed by the proposed new Insurance Contracts standard), we believe that there is substantive merit to align the mandatory effective date of these two standards. This would allow insurers to make informed decisions about their accounting policies, classification of financial instruments in view of the interaction between IFRS 9 and the proposed new Insurance Contracts standard whilst users' understanding of financial statements would be better preserved rather than having to grapple with sequential piecemeal fundamental changes year on year.

Doing so would also potentially minimise some of the accounting mismatches for insurers between assets and liabilities during a 2-step implementation approach and avoid the need for insurers to re-designate their financial instruments upon transition to the proposed new Insurance Contracts standard, after first implementing IFRS 9.

Field Test

We welcome the IASB's plans to undertake an additional round of field test for the proposals, in addition to the field tests conducted in 2009 and 2011, given the importance and implications of a first comprehensive standard for insurance contracts.

We hope that our comments will contribute to the IASB's deliberation on the 2013 ED. Should you require any further clarification, please contact our project managers Ivan Koo and Soon Lii Ang at their emails ivan_koo@asc.gov.sg and soonlii.ang@isca.org.sg respectively.

Yours faithfully

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Technical Director	Executive Director
Singapore Accounting Standards Council	Technical Knowledge Centre and Quality Assurance
	Institute of Singapore Chartered Accountants