25 November 2015

International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Sir,

Re: IASB Exposure Draft ED/2015/3 - Conceptual Framework for Financial Reporting

We appreciate the opportunity to comment on the Exposure Draft ED/2015/3 *Conceptual Framework for Financial Reporting* published by the International Accounting Standards Board (IASB). I am pleased to transmit, on behalf of the International Actuarial Association (IAA), our comments and recommendations.

These comments have been prepared by a task force appointed by the Insurance Accounting Committee and the Pensions and Employee Benefit Committee of the IAA. If, upon reading these comments, you identify any points that you wish to discuss or obtain further insight regarding them, please do not hesitate to contact William Hines, Chair of the Insurance Accounting Committee, care of the IAA Secretariat. The IAA will be pleased to develop these ideas further with you.

Yours sincerely,

Fred Rowley
President

Attachment: IAA comments

Comments by the International Actuarial Association on the IASB Exposure Draft ED/2015/3 - Conceptual Framework for Financial Reporting

International Actuarial Association and its Due Process

The International Actuarial Association (the "IAA") represents the international actuarial profession. Our sixty-seven Full Member actuarial associations, listed in Appendix A to this statement, represent more than 95% of all actuaries practicing around the world. The IAA promotes high standards of actuarial professionalism across the globe and serves as the voice of the actuarial profession when dealing with other international bodies on matters falling within or likely to have an impact upon the areas of expertise of actuaries.

We are pleased to be given the opportunity to provide input to the IASB on this important Exposure Draft. These comments have been prepared by the a task force appointed by the Insurance Accounting Committee and the Pensions and Employee Benefit Committee of the IAA, whose members are listed in Appendix B to these comments. It has also been subject to the due process required for it to constitute a formal view of the IAA, and will be posted to the IAA's official web site.

In the paragraphs below we provide responses to the questions posed in the Exposure Draft for which we feel we can make a meaningful contribution.

Question 1—Proposed changes to Chapters 1 and 2

Do you support the proposals:
(a) to give more prominence, within the objective of financial reporting, to the importance of providing information needed to assess management's stewardship of the entity's resources;

No comment.

(b) to reintroduce an explicit reference to the notion of prudence (described as caution when making judgements under conditions of uncertainty) and to state that prudence is important in achieving neutrality;

We agree with the concept of neutrality as it is laid out in the exposure draft. We believe it is important to focus on neutrality as prudence on its own is often interpreted as conservative, especially in the context of insurance and pensions. We believe a different word may be less subject to misinterpretation – such as care. As worded and as explained, the concept of prudence seems to lend support to a conservative bias in estimates, which we believe is not the intent of the Board.

(c) to state explicitly that a faithful representation represents the substance of an economic phenomenon instead of merely representing its legal form;

In the discussion there seems to be a blend of two concepts; economic vs. legal and substance over form. The legal construction of a contract often drives the economic basis. We feel the legal basis should be the first consideration in determining the economic substance. Certainly economic relationships may not always be defined by legal forms, because, for example, the economic substance of a relationship may require reference to several contracts or to separable parts of contracts, practices, and other environmental factors, such as regulation. So while we agree that faithful representation represents the substance of an economic phenomenon, we believe that the legal form is generally key to understanding the phenomenon and faithfully representing it. We caution against wording that emphasizes substance to the point of potentially too little regard for the legal form.

(d) to clarify that measurement uncertainty is one factor that can make financial information less relevant, and that there is a trade-off between the level of measurement uncertainty and other factors that make information relevant; and

Measurement uncertainty could but does not necessarily make financial information less relevant. We agree with what is stated in paragraphs 2.12 and 2.13. However, we believe that this discussion is incomplete, in that it does not distinguish between uncertainty that is inherent in what is being measured (risk inherent in the object), and uncertainty which resides in the measurement (estimation uncertainty).

Inherent risk typically resides in future values or events. It cannot be reduced by improved measurement. It is present in most economic activity and impacts financial information whenever it is necessary to provide a measure of future outcomes. It is particularly important in insurance, but can be material wherever there is risk.

Estimation uncertainty, in contrast, can, in principle, be reduced by better estimation techniques. This introduces a cost/benefit element into the discussion.

We also note that uncertainty, particularly inherent risk, may have its own relevance and that both faithful representation and relevance can be enhanced by measurement that appropriately reflects uncertainty.

Estimation uncertainty can sometimes be bypassed by historical measurement of something related (e.g. purchase price instead of estimating a current market price). Such avoidance is likely to result in financial information that is inferior in both faithful representation and relevance.

It would be helpful to recast 2.12 and 2.13, with the heading "Uncertainty", to distinguish between inherent risk and estimation uncertainty.

(e) to continue to identify relevance and faithful representation as the two fundamental qualitative characteristics of useful financial information? Why or why not?

No comment.

Question 2—Description and boundary of a reporting entity

Do you agree with:
(a) the proposed description of a reporting entity in paragraphs 3.11–3.12; and
(b) the discussion of the boundary of a reporting entity in paragraphs 3.13–3.25?
Why or why not?

Because the term "reporting entity" is used in determining the perspective for measuring many components of the entity, we believe more substance to the definition of the reporting entity would be useful. We believe the description included in RE2 of paragraph BC3.8, i.e. a "circumscribed area of economic activities" would be appropriate to bring into the definition of reporting entity in the Conceptual Framework itself. It might turn out to be insufficient to associate with a reporting entity only the function of providing reports, particularly if some IFRSs refer to its economic perspectives, e.g. the upcoming insurance standards, referring to the compensation which the reporting entity would require for bearing risks. Here, bearing the risks is an economic activity, which tags the reporting entity.

Question 3—Definitions of elements

Do you agree with the proposed definitions of elements (excluding issues relating to the distinction between liabilities and equity):

(a) an asset, and the related definition of an economic resource;

No comment.

(b) a liability;

We believe that the definition of a liability should focus on the transfer of control, not on transfer of the economic resource itself. The definition of economic resources does not include any indication as to who has the right to benefit from the resource, the phrase "transfer of economic resources" does not imply that there is a transfer of that right, i.e., control.

It is important that related assets and liabilities be measured in a manner consistent with each other to minimize distortions in reported income and performance measurement, resulting from inconsistent accounting measurements as circumstances change. Contracts can have asset and liability components that are measured on an integrated basis and could result in either a net asset or a net liability (e.g. in ED/2013/7 para. 54).

(c) equity;

No comment.

(d) income; and

No comment.

(e) expenses?

No comment.

Why or why not? If you disagree with the proposed definitions, what alternative definitions do you suggest and why?

Question 4—Present obligation

Do you agree with the proposed description of a present obligation and the proposed guidance to support that description? Why or why not?

No comment.

Question 5—Other guidance on the elements

Do you have any comments on the proposed guidance?
Do you believe that additional guidance is needed? If so, please specify what that guidance should include.

We support the flexibility afforded in the current exposure draft as we believe that unit of account should be addressed in the context of specific standard and is not necessarily fixed within the conceptual framework itself.

Question 6—Recognition criteria

Do you agree with the proposed approach to recognition? Why or why not? If you do not agree, what changes do you suggest and why?

We believe that the recognition criteria with regards to uncertainty needs to be enhanced. A high level of uncertainty does not presume irrelevance. We believe that when there are a number of events that individually would have a low level of certainty but in aggregate have a higher level of certainty should be recognized as they are relevant, for example, insurable events. Accordingly, in such a case, the recognition decision should not be determined solely at an item-by-item level but consider circumstances which might increase relevance and reduce the uncertainty. Such considerations should not be limited to measurement (as in IAS 37.39). We suggest an additional paragraph be added to address this issue. In addition we believe that the example in 5.21 should be modified to avoid being one-sided as it might be misleading.

While paragraph 5.13 is technically correct, we believe it would be helpful to clarify that it can be appropriate to recognize items even when there is a large range of potential outcomes. This would especially be the case if there are a number of significant items. Nonrecognition is

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tantamount to placing no value on something that may result in significant economic impact at a later date. If there are a number of such items, it may be fairly certain that there will be significant economic impact. At a minimum we believe the Board should consider requiring disclosures about the items, individually and collectively.

Question 7—Derecognition

Do you agree with the proposed discussion of derecognition? Why or why not? If you do not agree, what changes do you suggest and why?

No comment.

Question 8—Measurement bases

Has the IASB:
(a) correctly identified the measurement bases that should be described in the Conceptual Framework? If not, which measurement bases would you include and why?

No comment.

(b) properly described the information provided by each of the measurement bases, and their advantages and disadvantages? If not, how would you describe the information provided by each measurement basis, and its advantages and disadvantages?

No comment.

Question 9—Factors to consider when selecting a measurement basis

Has the IASB correctly identified the factors to consider when selecting a measurement basis? If not, what factors would you consider and why?

We are not aware of any issues with the factors identified by the IASB, however we have a small number of points of detail.

Sub-paragraph 6.54(b) notes that the characteristics of the asset or liability may suggest which measurement basis is most relevant and then goes on to give some examples of when that is the case. A further example that may be appropriate to include is the uniqueness of the asset or liability. For example fair value may be relevant where there are many similar, regularly traded contracts, but may be less relevant where the contract is a tailored one-off arrangement (as in case of most service contracts providing an individual service).

Paragraph 6.58 states that "… in some circumstances, using a similar measurement basis for related assets or liabilities may provide more useful information…" We agree with the intention

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behind that statement, however we suggest that it applies in most rather than just some circumstances and that it may be better to refer to "a consistent measurement basis" or "the same measurement basis" rather than "a similar measurement basis". Arguably fair value and fulfilment value are similar measurement bases because they are both current values, however those measurement bases may not be sufficiently similar. . Furthermore, the presentation in the statement of comprehensive income may be different, even if the measurement is similar. Again the insurance project provides an example of how options for treatment of the change in values of liabilities (through P&L or in OCI) and related assets provides consistent treatment (for example, FVPL compared to movement partly or entirely through P&L).

In some cases, assets or liabilities are not only "related" but the legal terms of one item refer directly to another item transferring its effect on the entity to a third party (cession or assignment). Typical examples are e.g. reimbursement rights, particularly reinsurance, or some policyholder participation rights (referring to the effects of the same and similar contracts). In such cases, even a "consistent measurement basis" is insufficient. E.g. the margin for risk and uncertainty decreases the value of assets but increases the value of liabilities. This would create a mismatch if applied to a legally off-setting relationship, such as reinsurance. It is necessary that the measurement (outcome) of the cession or assignment matches the measurement of the ceded or assigned item. To ensure matching measurement, the IASB decided that the reinsurance asset should be increased by a margin that matches the margin increasing the ceded liability, not decreased as it would be usual for assets.

In such cases, it is useful to revise the net position, when determining the treatment of legally offsetting items.

Question 10—More than one relevant measurement basis

Do you agree with the approach discussed in paragraphs 6.74–6.77 and BC6.68? Why or why not?

It has been a long standing view of the IAA that the valuation of assets and liabilities should be on a consistent basis. However, we understand there could be situations where a different approach may be used.

The approach in paragraphs 6.74 to 6.77 envisages different measurement bases for assets or liabilities and related income or expenses. It is also possible that there could be different measurement bases within a single asset or liability or applied in combination.

An example of an asset or liability that has more than one basis is a pension surplus or deficit that incorporates plan assets at fair value and a defined benefit obligation on a fulfilment value.

An example of a combination of measurement bases is the provision to compare a current value and historical cost to determine if there is an onerous liability, as set out in sub-paragraph 6.8(c).

We believe that it may be appropriate to add another paragraph noting that there may be other areas where there may be more than one relevant measurement basis.

Question 11—Objective and scope of financial statements and communication

Do you have any comments on the discussion of the objective and scope of financial statements, and on the use of presentation and disclosure as communication tools?

No comment

Question 12—Description of the statement of profit or loss

Do you support the proposed description of the statement of profit or loss? Why or why not?
If you think that the Conceptual Framework should provide a definition of profit or loss, please explain why it is necessary and provide your suggestion for that definition.

No comment.

Question 13—Reporting items of income or expenses in other comprehensive income

Do you agree with the proposals on the use of other comprehensive income? Do you think that they provide useful guidance to the IASB for future decisions about the use of other comprehensive income? Why or why not?
If you disagree, what alternative do you suggest and why?

We are concerned that the proposals on the use of other comprehensive income may be too restrictive and may not give due weight to the provision of relevant information to users of the financial statements.

We note that the Exposure Draft indicates that one of the purposes of the statement of profit and loss is to "provide information that is helpful in assessing prospects for future cashflows". Our understanding is that some users of financial statements will use a multiple of a measure of financial performance or similar approach to value a business. Those users need information that helps them assess the prospects for future earnings, consistent with the purpose discussed above.

The Exposure Draft indicates that income and expenses can be excluded from profit or loss where that would enhance the relevance. That provision could be taken to allow amounts to be excluded where those amounts are not consistent with assessing the future prospects of an organization, consistent with the purposes of profit or loss and our comments on the valuation of businesses above.

However, the strict requirements on the presumption that incomes and expenses will be included in the statement of profit or loss may not give sufficient weight to relevance.

Given that the Conceptual Framework is intended to guide the development of standards it may be more appropriate to avoid strict language like “cannot” and “can only” and make the points raised in paragraphs 7.23 and 7.24 guidance rather than strict requirements.

It may also be appropriate to explicitly allow the use of other comprehensive income where the income or expense is not consistent with the purpose of the statement of profit and loss set out in 7.20.

We were also concerned that paragraph 7.25 provides only one example of the provision in 7.24(a) and could be taken to limit the situations in which 7.24(a) applies. It may be helpful to add an additional paragraph that provides guidance on the application of 7.24(a). We understand that the purpose of 7.24(a) is to allow for income or expenses generated from a mismatch between measurement bases to be passed through other comprehensive income.

In some cases there may not be a specific statement about the mismatch. For example post-employment benefits accounted for under IAS 19 results in a surplus or deficit that is recognized as an asset or liability in an employer’s financial statement. The surplus or deficit is a combination of plan assets measured at fair value and a defined benefit obligation measured at something that is probably a fulfilment value. So a mismatch exists, and it is not clear that there is a single measurement basis for the gains or losses which relate to changes in plan assets and the defined benefit obligation.

Question 14—Recycling

Do you agree that the Conceptual Framework should include the rebuttable presumption described above? Why or why not?
If you disagree, what do you propose instead and why?

We do not agree that there should be a presumption that there will be reclassification of amounts included in other comprehensive income. The rebuttable presumption appears to be too restrictive and inconsistent with the role of the conceptual framework to provide guidance rather than set specific standards

We note that the purpose of the statement of profit or loss is to present the return earned by the entity during the period and to provide information that is helpful for assessing future cashflows. It is not clear that amounts recycled in some later period relate to the return earned during that later period or provide any information that would be helpful for predicting future cashflows.

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It may be appropriate for amounts to be reclassified if that enhances the relevance of the statement of profit or loss. However it is not clear that is the case sufficiently often for it to have such a presumption.

Hence we propose that 7.26 allow, but not require, reclassification to occur and that paragraph 7.27 be deleted. For example 7.26 could state:

If income or expenses are included in other comprehensive income in one period it may be reclassified into the statement of profit or loss in some future period when that will enhance the relevance of the information in the statement of profit or loss for that future period.

Question 15—Effects of the proposed changes to the Conceptual Framework

Do you agree with the analysis in paragraphs BCE.1–BCE.31? Should the IASB consider any other effects of the proposals in the Exposure Draft?

We believe the approach is sensible.

Question 16—Business activities

Do you agree with the proposed approach to business activities? Why or why not?

No comment.

Question 17—Long-term investment

Do you agree with the IASB's conclusions on long-term investment? Why or why not?

While we agree with a lot of the commentary set out in the basis for conclusions, we disagree with the IASB's conclusion that there is no need to add to the Conceptual Framework a specific reference on the needs of long term investors.

Our experience from working with long-term investors in the pensions and insurance areas is that long-term investors can sometimes find it difficult to access the information that they need from financial statements. Hence we support the comment in BCIN.43 that long-term investors may need additional disclosures.

Chapter 2 of the Conceptual Framework includes discussion on relevance. Given that different users will make different decisions on the basis of different criteria, we believe that it would be appropriate for the Conceptual Framework to recognise that as a factor when discussing relevance. That recognition need not distinguish between long-term and short-term investors as

the only distinction as there may be other categories of investors that also have different view on what represents relevant financial information.
We also believe that the discussion on disclosure in Chapter 7 could be enhanced by again mentioning the needs of different categories of users, given that it may be through disclosure that information is provided to satisfy the range of needs.

Question 18—Other comments

Do you have comments on any other aspect of the Exposure Draft? Please indicate the specific paragraphs or group of paragraphs to which your comments relate (if applicable).
As previously noted, the IASB is not requesting comments on all parts of Chapters 1 and 2, on how to distinguish liabilities from equity claims (see Chapter 4) or on Chapter 8.

Comments on APPENDIX A to the Exposure Draft

If the IASB decides to retain Appendix A we suggest that it should be expanded to adequately address each of the factors in cash-flow-based measurement techniques.

Paragraph A2 identifies a number of components in a cash-flow-based measurement. The appendix then introduces a sub-section that discusses variations in cashflows, the second sub-paragraph in A2.

There is no separate discussion on the time value of money or margin for risk and uncertainty which in our view are fundamental components of cash-flow-based measurement techniques. On that basis it seems that Appendix A is an incomplete discussion of cash-flow-based measurement techniques.

We also believe that, given the complexity of cash-flow-based measurement techniques and the choices available, it would be appropriate to make reference to consulting with experts when deciding on the appropriate techniques.

Appendix A

Full Member Associations of the IAA (67 members)
(25 November 2015)

Caribbean Actuarial Association
Consejo Profesional de Ciencias Económicas de la Ciudad Autónoma de Buenos Aires (Argentina)
Actuaries Institute Australia (Australia)
Aktuarvereinigung Österreichs (AVÖ) (Austria)
Institut des Actuaires en Belgique (Belgique)
Aktuarsko Drustvo U Bosni I Hercegovini (Bosnia and Herzegovina)
Instituto Brasileiro de Atuária (IBA) (Brazil)
Bulgarian Actuarial Society (Bulgaria)
Canadian Institute of Actuaries/Institut Canadien des Actuaires (Canada)
China Association of Actuaries (China)
Actuarial Institute of Chinese Taipei (Chinese Taipei)
Asociación Colombiana de Actuarios (Colombia)
Institut des Actuaires de Côte d'Ivoire (Côte D`Ivoire)
Hrvatsko Aktuarsko Drustvo (Croatia)
Cyprus Association of Actuaries (Cyprus)
Ceská Spolecnost Aktuárù (Czech Republic)
Den Danske Aktuarforening (Denmark)
Egyptian Society of Actuaries (Egypt)
Eesti Aktuaaride Liit (Estonia)
Suomen Aktuaariyhdistys (Finland)
Institut des Actuaires (France)
Deutsche Aktuarvereinigung e. V. (DAV) (Germany)
Hellenic Actuarial Society (Greece)
Actuarial Society of Hong Kong (Hong Kong)
Magyar Aktuárius Társaság (Hungary)
Félag Islenskra Tryggingastærðfræðinga (Iceland)
Institute of Actuaries of India (India)
Persatuan Aktuaris Indonesia (Indonesia)
Society of Actuaries in Ireland (Ireland)
Israel Association of Actuaries (Israel)
Istituto Italiano degli Attuari (Italy)
Institute of Actuaries of Japan (Japan)
Japanese Society of Certified Pension Actuaries (Japan)
The Actuarial Society of Kenya (Kenya)
Latvijas Aktuaru Asociacija (Latvia)
Lebanese Association of Actuaries (Lebanon)
Lietuvos Aktuaru Draugija (Lithuania)

Full Member Associations of the IAA (67 members)
…continued

Persatuan Aktuari Malaysia (Malaysia)
Colegio Nacional de Actuarios A. C. (Mexico)
Association Marocaine des Actuaires (Morocco)
Het Koninklijk Actuarieel Genootschap (Netherlands)
New Zealand Society of Actuaries (New Zealand)
Den Norske Aktuarforening (Norway)
Pakistan Society of Actuaries (Pakistan)
Actuarial Society of the Philippines (Philippines)
Polskie Stowarzyszenie Aktuariuszy (Poland)
Instituto dos Actuários Portugueses (Portugal)
Asociatia Romana de Actuariat (Romania)
Russian Guild of Actuaries (Russia)
Udruzenje Aktuara Srbije (Serbia)
Singapore Actuarial Society (Singapore)
Slovenska Spolocnost Aktuarov (Slovakia)
Slovensko Aktuarsko Drustvo (Slovenia)
Actuarial Society of South Africa (South Africa)
Institute of Actuaries of Korea (South Korea)
Col.legi d'Actuaris de Catalunya (Spain)
Instituto de Actuarios Españoles (Spain)
Svenska Aktuarieföreningen (Sweden)
Association Suisse des Actuaires (Switzerland)
Society of Actuaries of Thailand (Thailand)
Association of Consulting Actuaries (United Kingdom)
Institute and Faculty of Actuaries (United Kingdom)
American Academy of Actuaries (United States)
American Society of Pension Professionals & Actuaries (United States)
Casualty Actuarial Society (United States)
Conference of Consulting Actuaries (United States)
Society of Actuaries (United States)

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Appendix B

Members of the joint task force appointed by the Insurance Accounting Committee and the Pensions and Employee Benefit Committee of the IAA
(25 November 2015)

Robert Buchanan
Micheline Dionne
Stefan Engeländer
Dave Finnis
Yasuyuki Fujii
Tim Furlan
William Hines
Jason Melone
James B Milholland
Francis Ruygt
James F Verlautz
Derek Wright

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