



**ASSOCIATION ACTUARIELLE INTERNATIONALE
INTERNATIONAL ACTUARIAL ASSOCIATION**

June 19, 2009

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

Dear Sir

**Re: IAA comments on the IASB Discussion Paper *Preliminary Views on Revenue
Recognition in Contracts with Customers***

In response to the request for comments on the Discussion Paper *Preliminary Views on Revenue Recognition in Contracts with Customers* (the DP), I am pleased to transmit on behalf of the International Actuarial Association (IAA) our comments and recommendations.

These comments have been prepared by the Insurance Accounting Committee of the IAA. If, upon reading these comments, you identify any points that you wish to pursue, please do not hesitate to contact the chairperson of that Committee, Sam Gutterman, or any of the other members of the Committee. The IAA will be pleased to develop these ideas further with you.

Yours sincerely

Yves Guérard
Secretary General

[Attachment](#): IAA comments

A Commentary on the Discussion Paper
PRELIMINARY VIEWS ON REVENUE RECOGNITION IN CONTRACTS WITH CUSTOMERS
Released by the International Accounting Standards Board: December 2008

International Actuarial Association

The International Actuarial Association (the “IAA”) represents the international actuarial profession. Our sixty-two Full Member actuarial associations represent more than 95% of all actuaries practicing around the world. The Full Member associations of the IAA are listed in an Appendix to this statement. 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 on the areas of expertise of actuaries.

Due Process

The IAA is pleased to be given the opportunity to provide input to the IASB in the development of these important matters. These comments have been prepared by a task force of the Insurance Accounting Committee, the members of which are listed in an Appendix to this statement. 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.

General Comments

We support the boards’ effort to develop a standard on revenue recognition. We believe that a standard that narrows the range of practices and makes revenue recognition as uniform as possible among the different types of contracts has the potential to enhance the decision-usefulness of financial statements. Even if the boards are not able to adopt a single model for the revenue recognition, discussion of a standard will have provided valuable insights into the concepts of revenue recognition and related considerations.

Our letter focuses on how the principles in the DP might apply to insurance. Insurance contracts are complex, usually integrating transfer of insurance risk with many other performance obligations that include services and financial features. Considering how the principles can apply to insurance contracts is important, not only to insurers, as the considerations can inform the discussions related to other complex contracts.

At this time we do not express a view on whether insurance contracts should be in the scope of a general standard on revenue recognition. We will likely not come to a view until the boards’ discussions have progressed sufficiently that it is possible to fully analyze the effects of the model on insurance contracts and we can conclude if the financial information is more decision-useful than that provided by alternative models. Although the approach in the DP is not sufficiently robust to be applied to the full range of insurance products, we have developed our comments nonetheless as if insurance contracts will be in the scope of the standard.

Reconciling the Revenue Recognition Project to the Insurance Project

The boards have addressed the need to reconcile the insurance and the revenue recognition projects. Views expressed recently in the discussions regarding insurance contract accounting indicate movement towards consistency with the revenue recognition project.

The three components for measurement of performance obligations correspond to the three building blocks for measurement of insurance liabilities. The reconciliation of the projects depends on reaching consistent or compatible conclusions about the components or building blocks. There are significant issues that must be addressed for each component.

- Expected cash flows – for insurance these are the expected future benefits and expenses. A closely related topic is the inclusion of recurring premiums and certain discretionary benefits in the measurement. We are hopeful that the boards will conclude that all the expected future cash flows of the whole contract must be considered to properly measure the liabilities. We comment on the inclusion or exclusion of future premiums and discretionary features and on customer behaviour in our responses to Questions 3 and 4.
- Time value of money – we believe that the measurement of insurance liabilities must consider the time value of money. We comment on discounting in our response to Question 10(c).
- Margins – there are two key points, (1) whether the initial margin is calibrated to the consideration, or the present value of premium in the case of insurance, and whether there can be profit or revenue at issue; and (2) how should margin be allocated to stand-alone prices for separate deliverables. We would prefer that the boards reconcile the objectives of the margins for revenue recognition and for the measurement of liabilities. Our thoughts are presented in the responses to Questions 8 and 10(a) and (b).

The boards must also decide if re-measurement should be permitted, if not required, for the measurement of performance obligations. It is doubtful that the measurement of insurance liabilities, or any long-term liabilities for that matter, will provide decision-useful information if the effects of changing expectations for future cash flows are disregarded.

We encourage the boards to clarify how entities should distinguish changes in net obligations that relate to gains or losses and do not result in revenue recognition from changes that result in revenue recognition. For example, if an insurer is released from its obligation to provide protection because the policyholder terminates the contract prematurely (in exchange for an amount less than the recorded performance obligation), is the recorded performance obligation released as revenue or does the insurer recognize a gain?

We encourage the boards to address contracts with multiple components as soon as possible. The effect of unbundling may significantly affect insurers' revenue; however, the inter-relationship among components of many insurance products may make unbundling impractical.

Other issues

There are other issues that the boards must address before applying the transaction price model to insurance contracts. Especially important are:

- Identifying performance obligations or providing principles so that it is clear what they are;
- Determining when performance occurs, i.e., when an asset is transferred to the customer; and
- Treatment of the costs of obtaining the contracts.

Our comments on these and other topics are included in our responses to the questions for respondents, which follow.

Responses to questions for respondents

Question 1

Do you agree with the boards' proposal to base a single revenue recognition principle on changes in an entity's contract asset or contract liability? Why or why not? If not, how would you address the inconsistency in existing standards that arises from having different revenue recognition principles?

IAA Comment: We support the boards' effort to develop a single standard for revenue recognition that is based on changes in an entity's contract asset or contract liability. Revenue is presented as a fairly self-evident concept in both the Framework and in the DP. It would be helpful if the boards provide an expanded discussion of what they believe revenue represents.

We have not yet concluded whether or not the model proposed in the DP is better suited or more decision-useful for insurance contracts than other possible approaches. Our conclusion will depend, to a large extent, on how the concerns we express in the remainder of this paper are addressed either in the revenue recognition project or in the insurance project.

We also note that there are many widely varied types of insurance contracts, including relatively simple short duration contracts for which outcomes may not be known until well after the period of protection, contracts with multiple components, and those for which benefits are long-tailed but may not begin until many years after inception (e.g., deferred annuities). We look forward to working with the boards to determine how the proposed model might apply to all of these insurance contracts.

Question 2

Are there any types of contracts for which the boards' proposed principle would not provide decision-useful information? Please provide examples and explain why. What alternative principle do you think is more useful in those examples?

IAA Comment: As stated in our response to Question 1, we believe that a better understanding of how the proposed principle would apply to insurance contracts and analysis of the implications to the financial statements of insurers is needed before we can decide whether the

proposed principle would provide decision-useful information. Nevertheless, whether the principles are ultimately applied to insurance contracts or not, investigating how the principles can be applied to such highly complex and integrated contracts as insurance contracts could improve the understanding of the underlying concepts and result in a more general and widely applicable formulation of principles. Principles apparently suitable for relatively simple and less sophisticated products might prove to be inadequate for more complex contracts.

Question 3

Do you agree with the boards' definition of a contract? Why or why not? Please provide examples of jurisdictions or circumstances in which it would be difficult to apply that definition.

IAA Comment: We note that the definition is different from the definition found in IAS 32.13, which states that a contract is “an agreement between two or more parties that has clear economic consequences that the parties have little, if any, discretion to avoid, usually because the agreement is enforceable by law”. The boards should make it clear if they believe there is any substantive difference in the definitions, since the one in IAS 32 appears broader, more principle-based, and more consistent with the Framework. We are concerned that the definition in the DP leaves open the possibility that some cash flows, such as those related to certain discretionary features, would not be considered in the measurement of liabilities. We believe the definition should not preclude considering any expected obligation or right, not solely those that are strictly legally enforceable. We favor a definition that is consistent with the concept of the whole contract; i.e., one that leads entities to consider all expected future cash flows of contracts in the measurement of its liabilities and assets.

Question 4

Do you think the boards' proposed definition of a performance obligation would help entities to identify consistently the deliverables in (or components of) a contract? Why or why not? If not, please provide examples of circumstances in which applying the proposed definition would inappropriately identify or omit deliverables in (or components of) the contract.

IAA Comment: The definition is helpful, but we believe insurers will need supplemental guidance to determine how to apply the definition to what many view as the principal obligation of insurance, namely to provide protection against loss from insured events.

Protection is provided over the coverage period of the contract; i.e., the period during which the occurrence of the insured event results in a right of compensation and/or service. For many types of claims, the amount or timing of the payments or services to the customer may be uncertain for some time after the insured event has occurred. Hence, some actuaries believe that the performance obligation is not fully satisfied (and hence revenue is not completely recognized) until the time at which all uncertainty is resolved. Other actuaries believe that the protection provided during the period of coverage satisfies the performance obligation and that activities after the coverage period relate to delivery of the asset, not transfer of an asset.

As an example of the argument in favour of not fully recognizing revenue until claims are finally resolved and paid, consider a person who is protected against financial loss associated with disability from a sickness or an accident. Claim payments may extend for many months or years until the insured recovers from the disability or dies, or the benefit period ends. Similarly in the

case of general insurance, the insured event might have occurred, but the consequences are still uncertain to the insured and the insurer. This argument indicates that the protection continues until the claim becomes known and has been fully resolved.

As an example of the arguments in favour of recognizing revenue when claims are incurred rather than fully resolved, consider the situation of a customer insured against lawsuits. Once the event occurs that triggers the liability, the customer has an asset. The asset may have uncertain value, but the asset does exist and is relied upon by both the customer and other potential parties of the customer (such as potential buyers or creditors of the customer).

Insurance contracts with recurring premiums obligate the insurer to accept premiums and to continue coverage without the ability to re-price or re-underwrite the coverage. This obligation, which might include guaranteed insurability, might be a performance obligation that should be considered in revenue recognition. We note that taking this obligation into account raises the possibility that contracts are considered beyond the period of coverage purchased by paid premiums and until the point in time at which the insurer is no longer obligated to accept premiums. This point illustrates why it is not possible to limit consideration of insurance contracts with recurring premiums to those already paid. For example, if the first annual premium of a ten year contract has been paid, the insurer must reflect its obligation to accept premiums for nine additional years in order to properly determine its net contract position, even if the insurer can not require the policyholder to pay future premiums.

In some jurisdictions, the sale of an insurance product creates an obligation or contingent obligation with regard to various social mechanisms such as guaranty funds (to protect policyholders in the event of an insolvent insurers), residual market mechanisms (to subsidize or potentially subsidize certain portions of the market not voluntarily covered by insurers), or other social programs (such as government administered funds to provide coverage to victims of catastrophic accidents or illnesses). These items can be material and hence need to be considered in the price for an insurance product; yet they are not a good or service provided directly to the insurance customer. The definition of performance obligation in paragraph seems to ignore these items. We ask the boards to clarify if obligations to parties other than the customer are performance obligations affecting the recognition of revenue.

Question 5

Do you agree that an entity should separate the performance obligations in a contract on the basis of when the entity transfers the promised assets to the customer? Why or why not? If not, what principle would you specify for separating performance obligations?

IAA Comment: While we agree in principle with the concept, the application of the approach to insurance contracts will require specific guidance. Please see our discussion in our Question 8 response for more detail.

Question 6

Do you think that an entity's obligation to accept a returned good and refund the customer's consideration is a performance obligation? Why or why not?

IAA Comment: We believe that an entity’s obligation to accept a returned good is a performance obligation and that a portion of the consideration should be allocated to that obligation. The possible return of a contract is generally not a significant consideration for insurers. Nonetheless, we note that identifying the obligation to accept a returned good as a performance obligation requires reflecting customer behavior in the allocation of the transaction price to the stand-alone obligation. Reflecting customer behaviour is a concept that we have long supported in connection with the measurement of insurance liabilities.

Question 7

Do you think that sales incentives (e.g. discounts on future sales, customer loyalty points and ‘free’ goods and services) give rise to performance obligations if they are provided in a contract with a customer? Why or why not?

IAA Comment: We believe that sales incentives give rise to performance obligations if they are provided in a contract with a customer. Sales incentives in insurance contracts include items such as persistency bonuses (amounts added to a contract's values if the policyholder does not cancel his contract before a specified date) and “teaser” rates (amounts credited to a policyholder’s account in the first year at rates that exceed market rates as an inducement to purchase the contract). We believe that it is important that sales incentives are recognized as performance obligations that exist at the inception of the contract and that the consideration is allocated to these obligations at that time.

Question 8

Do you agree that an entity transfers an asset to a customer (and satisfies a performance obligation) when the customer controls the promised good or when the customer receives the promised service? Why or why not? If not, please suggest an alternative for determining when a promised good or service is transferred.

IAA Comment: We are inclined to agree, but we believe that insurers will require specific guidance for the application of this concept to insurance contracts. First, it is important that the general principle not be narrowed by limiting it to the two specific cases of goods or services. Insurance coverage cannot be simply identified with one or both, but the general principle can be applied nevertheless. The transfer that has taken place is the transfer of risk from the insured to the insurer. The idea that the performance obligation is the protection that is provided is difficult to express in terms of an asset that is transferred to the customer as the protection is provided.

In practice the issue is closely related to the requirement that the transaction price be allocated to the stand-alone price of the obligations. The stand-alone price for protection is based on the contract’s proportionate part of the expected incurred claims of the portfolio of contracts for the period.

In view of this perspective, revenue recognition for short duration contracts will be similar to an earned premium approach, except to the extent that it is decided that (1) some revenue is only recognized when claims are finally resolved; and (2) whether the degree of uncertainty in these incurred but unpaid claims should affect the revenue recognition pattern.

We note that the recognition of revenue for insurance contracts may involve the topic of the margin in performance obligations and in claims liabilities.

We see three alternatives with respect to margins and revenue recognition:

Revenue recognition period - alternatives	Margins	Comment
A. Revenue recognized only during (contract) coverage period	All margins in performance obligations relate to pre-claims. There are no margins in claims liabilities	Having no margins in claims liabilities is inconsistent with IAS 37. Revenue recognition is consistent with the concept that the performance is the protection that is provided
B. Revenue recognized only during (contract) coverage period	Margins are part of pre-claims performance obligations and there are margins for uncertainty in claims liabilities.	With no revenue remaining to be recognized as of the end of the coverage period, the expense for the claims includes an amount that is likely to be released into profit at a later date. However, it should be noted that a liability without a margin for uncertainty (if the cash flows are uncertain) is generally considered not to represent decision-useful information.
C. Some revenue recognized during coverage period and some during claims period	Margins relate to performance obligation (like unearned revenue) for pre- and post-claims performance obligations. Claims liabilities have no margins.	Revenue recognition may extend well beyond the coverage period. Margin in post claims period relates to unsatisfied performance obligation, not to claims liability. (Note that the claim liability that results would also not be consistent with IAS 37.)

These alternatives are illustrated in the attached appendix to these comments.

While it is common to associate a risk margin with a liability consisting of uncertain cash flows, we can see that alternative A may still be viewed by some as providing the most decision-useful information to the user. We are aware that such a measurement would not be in line with IAS 37, which requires some margin on top of the expected cost if the cost is subject to significant uncertainty. We believe the choice between alternatives B and C depends both on the identification of the deliverables in an insurance contract and on clarification of the objective of margins and their role in revenue recognition. A liability measurement for an uncertain set of cash flows may provide more decision-useful information if a margin is included to properly reflect the qualitative difference between a liability that is certain and one that is uncertain. On the other hand, including such a margin causes an additional expense that is expected to result in future gains when the margins are released. It should be noted that actual cash flows will likely differ from their corresponding expected value; therefore, there is typically a high probability of a gain. The margin would simply add to that gain and increase the probability that there is a

gain. However, the liability without a margin cannot be expected to provide decision-useful information. These are issues that are unresolved at this time. We offer our assistance to the boards as they deliberate these topics.

Question 9

The boards propose that an entity should recognize revenue only when a performance obligation is satisfied. Are there contracts for which that proposal would not provide decision-useful information? If so, please provide examples.

IAA Comment: We are not convinced that an entity should recognize revenue only when a performance obligation is satisfied. We note that the IASB has asked its staff to explore the possibility that revenue should be recognized at contract inception to the extent of incremental cost associated with obtaining the contract. We ask the boards to clarify whether they see this as an exception to the principle that an entity should recognize revenue only when a performance obligation has been satisfied or if they see it as consistent with the principle. If the boards see it as consistent, they should clarify if the allocation of the transaction price to performance obligations should consider these costs and should include a portion of the margin

We ask that the boards clarify how entities should distinguish changes in net obligations that relate to gains or losses and does not result in revenue recognition from changes that result in revenue recognition. For example, if an insurer is released from its performance obligation because the policyholder terminates the contract prematurely (that is, in exchange for an amount less than the recorded performance obligation), is the remaining performance obligation released as revenue or does the insurer recognize a gain?

We also believe that in the case of insurance, these incremental costs are not transaction costs, but costs incurred containing a service that is an integral part of the contract's performance, and therefore the recognition of revenue is in compliance with the principle.

In other respects we believe this question will be answered by a resolution of the issues presented in our response to Questions 8 and 10.

Question 10 (a)

In the boards' proposed model, performance obligations are measured initially at the original transaction price. Subsequently, the measurement of a performance obligation is updated only if it is deemed onerous.

(a) Do you agree that performance obligations should be measured initially at the transaction price? Why or why not?

IAA Comment: We ask that the boards seek to articulate how the calibration of margins to the consideration is consistent with the principles of the measurement of liabilities. The boards should clarify what the residual margin (the margin in excess of the price for risk and service) represents in the measurement of liabilities. Note that we might be convinced that a calibration to the transaction price at initial measurement might be reasonable and justified in the absence of a sufficient level of positive evidence for any initial gain.

Question 10 (b)

Do you agree that a performance obligation should be deemed onerous and re-measured to the entity's expected cost of satisfying the performance obligation if that cost exceeds the carrying amount of the performance obligation? Why or why not?

IAA Comment: We note that this issue is related to the issue of re-measurement. With re-measurement of the performance obligations, the liability will always reflect current estimates of future cash flows (see our response to Question 10 (d)). There may not be a need for specific testing for onerous contracts.

If there were to be a test for onerous insurance contracts, then the test should be made for groups of contracts with similar risk characteristics, to avoid the impression that an individual contract is onerous if there is a claim.

When re-measurement is not performed, we agree that a performance obligation whose expected cost exceeds the carrying amount should be deemed onerous in any case. We agree that including a margin in the measurement of an onerous liability creates an expense that is likely to be reversed into profit and loss in a future period. See our discussion in the response to question 8 on the topic of margins.

Question 10 (c)

Do you think that there are some performance obligations for which the proposed measurement approach would not provide decision-useful information at each financial statement date? Why or why not? If so, what characteristic of the obligations makes that approach unsuitable? Please provide examples.

IAA Comment: Our response to this question depends in part on the resolution of the issues we raise in response to Question 4 and 8 and in part (d) (below) of this question.

Question 10 (d)

Do you think that some performance obligations in a revenue recognition standard should be subject to another measurement approach? Why or why not? If so, please provide examples and describe the measurement approach you would use.

IAA Comment: Our response depends on how "original transaction price" is defined; for example, whether or not it includes the present value of expected future cash flows resulting from certain long-duration contracts. We believe that it is essential that there be discounting and re-measurement for such long-duration contracts.

Measuring performance obligations without considering the time value of money is not consistent with the pricing of long term obligations. The recognition of revenue for contracts with long term obligations is potentially materially different if there is no discounting. Not discounting may significantly overstate the value of the obligations, could result in lower apparent margins and could give the appearance that contracts are onerous. Take the case of a 20 year single premium term life insurance contract, i.e., a life insurance contract with a lump sum cash payment in case of death within twenty years, which is purchased for a single initial premium payment. The expected cost, without consideration of time value of money, could

easily exceed the market premium by a significant amount. Consequently, without discounting, issuing such a contract for a market price would usually result in reporting a loss at inception that is entirely recovered over the next 20 years.

When expected future performance obligations are revised, the total remaining unrecognized revenue should be reallocated to future periods to reflect current expectations. This approach provides more relevant information about performance that has been provided and performance that is yet to be provided. We do not believe that re-measurement should have cumulative effects because we do not believe that revenue in the current period should reflect redistribution of revenue already recognized in prior periods.

Users should be informed if an insurer revises the future remaining performance pattern and consequently the future expected revenue, not only if contracts are onerous.

The boards should also address how deviations in experience from expectations should be reflected in profit and loss. Are there gains or losses in contracts from these deviations, or are revenue and expenses directly affected?

Question 11

The boards propose that an entity should allocate the transaction price at contract inception to the performance obligations. Therefore, any amounts that an entity charges customers to recover any costs of obtaining the contract (e.g., selling costs) are included in the initial measurement of the performance obligations. The boards propose that an entity should recognize those costs as expenses, unless they qualify for recognition as an asset in accordance with other standards.

(a) Do you agree that any amounts an entity charges a customer to recover the costs of obtaining the contract should be included in the initial measurement of an entity's performance obligations? Why or why not?

IAA Comment: Acquisition costs for insurance contracts are significant enough to the cash flows of the contract that including the amounts intended for the recovery of these costs in the initial measurement of the performance obligations may represent a material distortion of the obligation. We hope the boards will permit the recognition of revenue at inception in order to cover the expense for the costs of obtaining the contract.

Question 11 (b)

In what cases would recognizing contract origination costs as expenses as they are incurred not provide decision-useful information about an entity's financial position and financial performance? Please provide examples and explain why.

IAA Comment: Please refer to our response to Question 11 (a).

Question 12

Do you agree that the transaction price should be allocated to the performance obligations on the basis of the entity's stand-alone selling prices of the goods or services underlying those performance obligations? Why or why not? If not, on what basis would you allocate the transaction price?

IAA Comment: In the context of the principles of the proposed model, we believe the allocation process is not appropriate in all cases. We note that there are frequently other considerations and interrelationships between the various obligations under a contract that may make stand-alone prices for unbundled services not directly comparable.

We suggest that the boards address in general whether the stand-alone price of the deliverables includes a risk margin or whether the risk margin is subsumed by the margin that arises from the calibration to the transaction price. In the discussions related to the insurance project, the IASB staff has referred to a residual margin for the former approach and a composite margin for the latter approach. We believe that the stand-alone price for a performance obligation should include the margin that would be associated with that performance obligation. Hence amount that calibrates the transaction price to the sum of the prices for the separate performance obligations will be a residual margin.

We note that the residual margin may be positive or negative. A negative margin may indicate that a contract is onerous depending on the definition of onerous. Please refer to our response to Question 10(b) for our comments on margins in connection with onerous contracts.

We also note that the residual margin will implicitly account for all differences between the entity's pricing methodologies and the pricing of the performance obligations. For example, the standard may not permit insurers to consider spreads above risk-free rates that they anticipate from their investments, but the insurer's pricing of the contracts may consider these spreads. The difference in the present values of cash flows caused by the differing discount rates will be reflected in the residual margin.

Question 13

Do you agree that if an entity does not sell a good or service separately, it should estimate the stand-alone selling price of that good or service for purposes of allocating the transaction price? Why or why not? When, if ever, should the use of estimates be constrained?

IAA Comment. Although we agree in concept, it may be difficult for insurers to calculate the stand-alone price of goods or services for purposes of allocating the transaction price. The application of the transaction price model depends on identifying the obligations to be priced (see Question 4) and on developing appropriate pricing techniques. Contracts may be priced holistically, so pricing separated deliverables will require developing new techniques.

Further, the deliverables may also relate to obligations, for example the guarantee to accept future premiums, which insurers have not priced as stand-alone obligations in the past. Insurance contracts may be priced as bundles of cash flows, without separate pricing of cash flows that relate to deposit features.

We believe that if a large difference between the sum of the prices of the individual good and services and the transaction price for the entire contract arises, the basis for determining why it is reasonable to assume that there is a large market discount or pricing premium associated with the combination of the goods or services should be provided.

Appendix A

APPENDIX A (actual claims = expected)							
	Coverage period				Post coverage period		
	1	2	3	4	5	6	
Consideraton	120						
Expected claims	25	25	25	25			
Actual Claims							
incurred	25	25	25	25			
paid			25	25	25	25	
Option A							
Allocation of transaction price							
claims incurred *	30	30	30	30			
claims uncertainty **	0	0	0	0			
End of period							
Performance obligation	90	60	30	0			
Claims liability- no margin	25	50	50	50	25	0	
P&L							Total
Revenue	30	30	30	30	0	0	120
Claims expense							
incurred - initial	-25	-25	-25	-25			-100
incurred - change in estimate		0	0	0	0	0	0
P&L	5	5	5	5	0	0	20
Option B							
Allocation of transaction price							
claims incurred *	30	30	30	30			
claims uncertainty **	0	0	0	0			
End of period							
Performance obligation	90	60	30	0			
Claims liability - margin of 8%	27	54	54	54	27	0	
P&L							Total
Revenue	30	30	30	30	0	0	120
Claims expense							
incurred - initial	-27	-27	-27	-27			-108
incurred - change in estimate		0	2	2	2	2	8
P&L	3	3	5	5	2	2	20
Option C							
Allocation of transaction price							
claims incurred *	28	28	28	28			
claims uncertainty **			2	2	2	2	
End of period							
Performance obligation	92	64	34	4	2		
Claims liability - no margin	25	50	50	50	25	0	
P&L							Total
Revenue	28	28	30	30	2	2	120
Claims expense							
incurred - initial	25	-25	-25	-25			-100
incurred - change in estimate		0	0	0	0	0	0
P&L	3	3	5	5	2	2	20
Option A has all revenue and claims expense in the period of coverage. If actual claims equal expected, then there is no profit or loss after the coverage period.							
Option B has all revenue and expense in the period of coverage. The expense includes accrual for a margin on the claims liability. There is no revenue after the coverage period, but some profit is deferred until the uncertainty related to claims is cleared. Profit is the gain on the claims runoff which equals the margin if actual claims are equal to expected.							
Option C has some revenue related to the obligation to take on the uncertainty related to claims. Revenue recognition extends beyond the coverage period. The claims expense is the same as option A, there is no gain or loss on runoff. The profit and loss is the same as option B, but the profit after the coverage period arises from the revenue recognized in the runoff period and the fact that the actual cost for uncertainty is nil.							

Appendix B

APPENDIX B (actual claims 80% of expected)							
	Coverage period				Post coverage period		
	1	2	3	4	5	6	
Consideration	120						
Expected claims	25	25	25	25			
Actual Claims							
incurred	20	20	20	20			
paid			20	20	20	20	
Option A							
Allocation of transaction price							
claims incurred *	30	30	30	30			
claims uncertainty **	0	0	0	0			
End of period							
Performance obligation	90	60	30	0			
Claims liability- no margin	20	40	40	40	20	0	
P&L							Total
Revenue	30	30	30	30	0	0	120
Claims expense							
incurred - initial	-20	-20	-20	-20			-80
incurred - change in estimate		0	0	0	0	0	0
P&L	10	10	10	10	0	0	40
Option B							
Allocation of transaction price							
claims incurred *	30	30	30	30			
claims uncertainty **	0	0	0	0			
End of period							
Performance obligation	90	60	30	0			
Claims liability - margin of 8%	21.6	43.2	43.2	43.2	21.6	0	
P&L							Total
Revenue	30	30	30	30	0	0	120
Claims expense							
incurred - initial	-21.6	-21.6	-21.6	-21.6	0	0	-86.4
incurred - change in estimate		0	1.6	1.6	1.6	1.6	6.4
P&L	8.4	8.4	10	10	1.6	1.6	40.0
Option C							
Allocation of transaction price							
claims incurred *	28	28	28	28			
claims uncertainty **			2	2	2	2	
End of period							
Performance obligation	92	64	34	4	2		
Claims liability - no margin	20	40	40	40	20	0	
P&L							Total
Revenue	28	28	30	30	2	2	120
Claims expense							
incurred - initial	-20	-20	-20	-20			-80.0
incurred - change in estimate		0	0	0	0	0	0.0
P&L	8	8	10	10	2	2	40.0
Option A has all revenue and claims expense in the period of coverage. If actual claims equal expected, then there is no profit or loss after the coverage period.							
Option B has all revenue and expense in the period of coverage. The expense includes accrual for a margin on the claims liability. There is no revenue after the coverage period, but some profit is deferred until the uncertainty related to claims is cleared. Profit is the gain on the claims runoff which equals the margin if actual claims are equal to expected.							
Option C has some revenue related to the obligation to take on the uncertainty related to claims. Revenue recognition extends beyond the coverage period. The claims expense is the same as option A, there is no gain or loss on runoff. The profit and loss is the same as option B, but the profit after the coverage period arises from the revenue recognized in the runoff period and the fact that the actual cost for uncertainty is nil.							

Appendix C

APPENDIX C (actual claims 120% of expected)							
	Coverage period				Post coverage period		
	1	2	3	4	5	6	
Consideration	120						
Expected claims	25	25	25	25			
Actual Claims							
incurred	30	30	30	30			
paid			30	30	30	30	
Option A							
Allocation of transaction price							
claims incurred *	30	30	30	30			
claims uncertainty **	0	0	0	0			
End of period							
Performance obligation	90	60	30	0			
Claims liability- no margin	30	60	60	60	30	0	
P&L							Total
Revenue	30	30	30	30	0	0	120
Claims expense							
incurred - initial	-30	-30	-30	-30			-120
incurred - change in estimate		0	0	0	0	0	0
P&L	0	0	0	0	0	0	0
Option B							
Allocation of transaction price							
claims incurred *	30	30	30	30			
claims uncertainty **	0	0	0	0			
End of period							
Performance obligation	90	60	30	0			
Claims liability - margin of 8%	32.4	64.8	64.8	64.8	32.4	0	
P&L							Total
Revenue	30	30	30	30	0	0	120
Claims expense							
incurred - initial	-32.4	-32.4	-32.4	-32.4	0	0	-129.6
incurred - change in estimate		0	2.4	2.4	2.4	2.4	9.6
P&L	-2.4	-2.4	0	0	2.4	2.4	0.0
Option C							
Allocation of transaction price							
claims incurred *	28	28	28	28			
claims uncertainty **			2	2	2	2	
End of period							
Performance obligation	92	64	34	4	2		
Claims liability - no margin	30	60	60	60	30	0	
P&L							Total
Revenue	28	28	30	30	2	2	120
Claims expense							
incurred - initial	-30	-30	-30	-30			-120.0
incurred - change in estimate		0	0	0	0	0	0.0
P&L	-2	-2	0	0	2	2	0.0
Option A has all revenue and claims expense in the period of coverage. If actual claims equal expected, then there is no profit or loss after the coverage period.							
Option B has all revenue and expense in the period of coverage. The expense includes accrual for a margin on the claims liability. There is no revenue after the coverage period, but some profit is deferred until the uncertainty related to claims is cleared. Profit is the gain on the claims runoff which equals the margin if actual claims are equal to expected.							
Option C has some revenue related to the obligation to take on the uncertainty related to claims. Revenue recognition extends beyond the coverage period. The claims expense is the same as option A, there is no gain or loss on runoff. The profit and loss is the same as option B, but the profit after the coverage period arises from the revenue recognized in the runoff period and the fact that the actual cost for uncertainty is nil.							

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