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Austrian Comments on the ED 5 Insurance Contracts issued by the IASB for Consultation

Vienna, dated 27. 10. 2003

Dear Mr. Clark,

the Austrian Insurance Association (VVO) represents all private insurance companies operating on the Austrian market, with the exception of the small mutual companies. The VVO is following the discussions on the project to design a new accounting standard for insurances very closely and with a great attention.

The VVO has participated actively in the respective Working Party formed in the Comité Européen des Assurances (CEA) in developing its comments. We therefore support the respective CEA-paper on the ED 5 as it stands. Nevertheless we allow to forward to you the enclosed Austrian Position Paper prepared by the Working Party of the VVO, which applied a different approach in analysing the ED 5.

We tried to take care in the single comments to point out our agreement and our disagreement, whatever applies. In addition to that we tried to explain, why we are taking a certain view, so that a third person can understand it.

Yours faithfully,

Verband der Versicherungsunternehmen
Österreichs

Dr. Louis Norman

Enclosure

Peter_Clark_Brief

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Position Paper of the Austrian Insurance Association (VVO) on the Exposure Draft 5 (ED 5) for Insurance Contracts of the IASB

Instead of a Foreword

Allgemein Bürgerliches Gesetzbuch (ABGB) Österreichs aus dem Jahre 1811, Versicherungsvertrag § 1288:

Wenn jemand die Gefahr des Schadens, welcher einen Andern ohne dessen Verschulden treffen könnte, auf sich nimmt, und ihm gegen einen gewissen Preis den bedungenen Ersatz zu leisten verspricht; so entsteht der Versicherungsvertrag. Der Versicherer haftet dabei für den zufälligen Schaden, und der Versicherte für den versprochenen Preis.

General Civil Code (ABGB) from Austria dated 1811, Insurance Contract § 1288:

If somebody takes the danger of loss, which could hit somebody else without its fault, and promises against the payment of a certain price to pay for convened damages; an insurance contract evolves. The insurer is liable for casual losses, and the insured is liable to pay the promised price.

In response to your request to make comments to ED 5 the Austrian Insurance Association (Verband der Versicherungsunternehmen Österreichs = VVO) is pleased to submit the views of the Austrian insurance industry. The comment is divided in two sections: Section 1 to the draft of the IFRS and section 2 to the paragraphs 7 to 61 of the Implementation Guidance.

Section 1: Comments to the Exposure Draft Issues

To paragraph 1: Objective – subparagraph b

In the opinion of the VVO the objective stated in paragraph 1, subparagraph b "…. to give users …. insights …. *without imposing costs that exceed the benefits and at a reasonable, but not excessive, level of aggregation*" is not transposed by the disclosure rules, which in the opinion of the VVO are excessive (we refer to the comments given in Section 2 to the Draft Implementation Guidances Issues).

To paragraphs 2 to 4: Scope (Questions 1 and 2)

To paragraph 2: subparagraph (a)

The Austrian Insurance Association (VVO) does not object to the decision taken in ED 5 that the accounting principles for insurance contracts apply to contracts regardless by whom they are issued, and are not restricted to certain industries (especially insurance companies).

Even though the exposure draft on insurance contracts will be applicable to insurance contracts regardless by whom they are issued, it must be taken into consideration that the principles laid out in the exposure draft are primarily of importance for insurance companies. Therefore the principles to distinguish between insurance contracts and other contracts should foresee, that (only) in case of doubt any contract issued by an insurance company (regarded as an insurer for legal or supervisory purposes) is an insurance contract.

To paragraph 2: subparagraph (b)

The VVO does not see reasons, why the IFRS shall also be applied to financial instruments issued with a discretionary participation feature.

To paragraph 3

According to paragraph 3 of the IFRS an Insurance Contract shall not address aspects of accounting for financial assets held by insurers; it seems to be intended by the IASB to measure the financial investments according to the rules of IAS 39 without any exception for investments covering insurance liabilities.

It can be expected that IAS 39 in its final version will require that all financial assets are measured at fair value; according to the principles laid down in the draft of the IFRS on Performance Reporting (Comprehensive Income) also unrealised gains and losses will have to be included in the income statement.

If the financial assets are measured at fair value and the changes of unrealised results are included in the income statement and the insurance liabilities on the other hand are valued at amortised costs, changes of unrealised results in the investments lead to profits and losses in the income statements; losses are shown even if the premiums and liabilities are calculated using an interest rate which is equal to the interest rate of the company's asset portfolio unless the interest rate used for the measurement of the liabilities is linked to the market interest rate. In the opinion of the VVO it would not be reasonable if every change in the market interest rate should result in a change of the interest rate which is used for the measurement of the (discounted value) of the insurance liabilities.

The so-called mismatch of the measurement principles for insurance assets and liabilities is in the opinion of the VVO a material problem only for the disclosure of the performance of the pure endowment insurance.

The VVO refuses to treat insurance contracts for accounting purposes in the same way as long term investment contracts and other financial instruments, because insurance contracts are service contracts: Insurers knowingly cover the financial effects of uncertain events not influencable by them and bear the risk of their occurrence. The IFRS on insurance contracts should therefore be designed in a manner to meet the principles of revenue recognition which have to be applied by other enterprises working in the service industry. The VVO identifies a deficiency in the discussions and considerations relating to accounting principles of insurance contracts therein that the persons developing those principles may have primarily in mind certain kinds of life insurance and thus have drawn the wrong conclusion that insurance contracts are financial instruments or are at least in close relation to them.

As the VVO refuses the measurement of insurance liabilities at fair value, the transitional provisions in paragraph 35 of ED 5 (which allow the insurers to reclassify some or all financial assets into the category of assets measured at fair value with changes of fair value recognised in profit and loss if the insurer changes the accounting principles for insurance contracts permitted by paragraph 14[1]) does not bring a solution of the problem.

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1 this means probably to change the measurement of insurance liabilities to the fair value-principle

Therefore the VVO proposes that special measurement and disclosure rules for investment held to cover insurance liabilities should be included either in the IFRS for insurance contracts or in the IAS 39. These special rules should permit

– to measure interest bearing investments at amortised cost without applying the strong tainting rules of IAS 39 for financial instruments classified as held to maturity and
– not to include unrealised gains and losses relating to shares and other equity instruments as well as to investment property which are not classified as "held for trading" into the income statement as part of the performance of the financial year.

Such regulations would avoid arbitrary fluctuations of the annual results caused by the mismatch arising from different measurement principles for insurance investments and insurance liabilities if the latter are not measured at fair value.

The VVO is aware of the fact, that a distinction between the treatment of unrealised gains and losses arising from insurance investments does not meet the intentions of the IASB laid down in ED 5. The VVO thinks, however, that accounting rules should not be governed by theoretical principles and the principle of uniform treatment of subjects which are not really comparable but by the usefulness of the financial statements for its users (in the case of insurance enterprises not only investors but also policyholders and supervisory authorities).

The VVO wants to indicate, that even if interest bearing investments are measured at amortised costs the – often random – fluctuations of fair values of investments in equity instruments influence the performance of an insurer if the unrealised results of these investments are recognised in the income statement. These effects cannot be removed by changing the interest rates used in the measurement of the insurance liabilities because the changes of the prices of shares are – as the experience in the last years showed – not primarily induced by changes of the interest rates but by other – sometimes irrational – reasons.

In the opinion of the VVO fluctuations of the market values of investments in equity instruments influence the performance, but do not distort them. This is due to the fact that the changes in the value of these investments are the consequence of investment decisions in the past where it turns out now whether they have been beneficial or not. A reversal of the changes in the market values of these investments in the future until maturity is not predictable as it is in the case of interest bearing investments. In the opinion of the VVO it would be preferable to include the unrealised gains and losses in a special item (reserve) within equity and to show the changes of this reserve as a special item on the face of the income statement, if the unrealised results are included in this statement.

For the sake of completeness the VVO points out, that unrealised results – especially unrealised gains – of investments which cover liabilities from insurance contracts with policyholder participation features have to be presented primarily as liability (deferred portion of the policyholders' rights for profit participation) and not as equity.

To Appendix B paragraph 18, subparagraph g: (Question 1 b)

The VVO has no objection, that contracts which foresee payments to a contractual party in the case of the occurrence of a certain weather-constellation, where the weather does not implicate advantages or disadvantages for the contractual partner, are not classified as an insurance contract; in this case the contracts qualify as "games and bets". Therefore the question should be raised, why these kinds of contracts are explicetly exempted from the scope of insurance contracts as they are anyway not meeting the definition of an insurance contract as outlined in Appendix A. In the comments should be explained – if weather-contracts are mentioned explicetly – that a weather-insurance-contract is not only given, if the insured suffers calculable financial losses in the case of a certain weather-situation, but also, if the occurrence of a certain weather-event (i.e. rain or lack of snow) induces the insureds an adverse effect of their expectations (recreation-value) and the insurance payment presents a compensation for the suffered expectation loss.

To appendix B, paragraphs 17 and 18: (Question 2)

In the opinion of the VVO the distinction between insurance and financial contracts, which are classified as financial instruments, can only create problems in the field of life insurance contracts. Financial investment contracts are only possible in case of:

– Whole life and endowment insurance contracts (combined death-survival-insurance) against single premium payment and short duration or increasing death/survival benefit.

– Whole life and endowment insurance contracts (combined death-survival-insurance) with regular premium, if the benefit out of the contract increases in analogy to the totally earned premiums including investment returns.

– Deferred annuity contracts, whereby the policyholder will receive, or can opt to receive a life-contingent annuity at rates prevailing when the annuity payments begin.

– Annuity contracts in the disbursement phase, if the duration of the annuity payment is limited and in case of an early death of the insured a minimum benefit has to be paid to the heirs.

It should be stated in the appendix, that in all these cases financial insurance contracts only exist if the difference between the highest and lowest benefit payable to the policyholders does not reach a certain percentage (e.g.5 %[2]) of either the maximally or minimally payable amount. In such a comparison not only the benefits payable to the policyholder but also the interests accumulating between the date of the acquisition of the insurance contracts and the possible dates of payments of the benefits have to be taken into consideration if the payments are due at different times.

To paragraphs 5 and 6: Embedded derivatives (Question 3)

The VVO is of the opinion that all benefits of the insureds resulting from insurance contracts and the related risks are part of the insurance contract itself, and that they have to be considered in the measurement of the liabilities. Therefore the VVO does not understand that

2 Regarding the percentage, discussions with actuaries should be held; it would also be possible to restrict such a quantitative limit to contracts issued by insurance companies (see also the proposal to question 1 that in case of doubt contracts issued by insurance companies should be classified as insurance contracts)

for certain risks (arising from embedded derivatives) measurement should be carried out in accordance with IAS 39. Even without such an indication it should be clear to measure exceptional and for an insurance contract untypical benefits and risks according to the principles of other corresponding IAS.[3]

This statement is independent of the principle under which liabilities are measured. The fact, that in paragraph IG 14 of the Implementation Guidance 18 examples are cited for the decision whether an embedded derivative should be valued separately or not, proves that the proposed solution is extremely casuistic.

The VVO cannot understand why the risk of a sudden death in pure endowment insurance or a long survival in annuity insurance should be a financial risk; it is the elementary insurance risk inherent in a life insurance contract. Also the consideration of a minimal return of investment defining the benefit of an endowment or annuity insurance is an integral part of a life insurance contract and decisive for the calculation of the premium and the benefit. If it turns out that the interest rate of the calculation was too high and the danger emerges, that the return of investment would not reach the calculated return, a typical situation is created where a provision for premium deficiency and unexpired risk must be recognised.

Concerning the example 1.4 in IG 2 in the opinion of the VVO also temporary annuities create a significant risk exposure for the insurer since in the calculation of the annuity the probability of the death of the annuitant in the period, for which the annuity is paid, is considered. Therefore there is a possibility of loss if the annuitant survives until the end of the annuity payments. An insignificant insurance risk would only exist in the case of a temporary annuity, if the period of the annuity payments is so short that the probability of death is very low.

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3 An example of such an atypical risk could be seen, if in such a contract the amount of the benefit depends on the growth of share prices, indices or other market prices and at the same time a minimum insurance benefit is guaranteed; this means, that it is not an unit linked insurance, where the policyholder bears all risks and opportunities arising from the linked investment.

To paragraphs 54 and 58 of the implantation guidance

The obligation to comment in the notes on the amount of the loss risks, as required by IG 54 and IG 58 is considered by the VVO as very problematic. It may make sense to provide information about the interest rates used in the calculation of the premiums and in the calculation of technical provisions and to show the effects on profit, if the interest rate which forms the basis for the measurement of insurance liabilities for life insurance contracts increases or decreases by a certain percentage due to a change of the forecasted future investment profits (sensitivity analysis).

To paragraphs 9 and 10: Temporary exemption from some other IFRS (Question 4)

To paragraph 9

The VVO is of the opinion that there should be no time-lag between the principle laid down in paragraph 9 of the ED 5 and the final IFRS-I. The VVO assumes, however, that the exemption of the use of certain stipulations of IAS 8 will be extended, if by the 1st of January 2007 the final Insurance Standard (phase II) will not be in place.

To paragraph 10

In principle there is no objection against the decision not to state positively in ED 5, which accounting principles and rules should be applied until the IFRS-I is finalised, but instead to set up certain specific rules (no equalisation and catastrophe-provision, execution of a loss recognition test, no derecognition of insurance liabilities until they are completely extinguished) and limit possible changes from the existing accounting principles (see comments to paragraphs 14 to 17).

To paragraph 10 subparagraph (a)

As to the prohibition to recognise equalisation and catastrophe provision the VVO wants to point out that there are very suitable reasons for such provisions in the attempt to present the correct result for an accounting period, as the period of one year is not long enough to equalise the risk fluctuations according to the law of big numbers, which is the basis for every insurance activity in an effective manner. The VVO is, however, conscious of the fact, that the “correct” calculation of such provisions is a complicated task and therefore accepts the fact of its prohibition in ED 5. In the opinion of the VVO the fact that the liabilities are not regarded as real liabilities in the sense of the IAS-Framework, is, however, not a suitable justification for not recognising an objectively necessary accrual and equalisation item.

To paragraph 10 subparagraph (b)

The VVO asks for additional guidance on how a loss recognition test must be conducted; in particular it should be clarified, whether such a test has to be carried out on the basis of the entire portfolio of insurance contracts or of specific groups of insurance contracts or of other defined business areas, since the result of such a test highly depends on the chosen basis.

In the opinion of the VVO it would be reasonable to treat the issue of measuring provisions for premium deficiency and unexpired risk (in the form of a separate provision, a write-down of assets or an increase of the insurance liabilities measured according to the companies' accounting principles) already in phase I, as the recognition of such a provision is already required by accounting principles in force; there are, however, different perceptions about the applicable procedures. In this regard the VVO expresses its doubts whether the rules laid down in IAS 37 are appropriate for the calculation of provisions for premium deficiency and unexpired risk for insurance contracts.

To Paragraphs 14 to 17: Changes in Accounting Policies (Question 5a)

To paragraph 14

The VVO expresses its concerns regarding the possibility to allow insurance companies to change their accounting policies during the transition period until phase II is in place if such a change "makes the financial statements more relevant to the decision-making needs of users and reliable, judged by the criteria in IAS 8". At present the financial statements of most insurance groups are prepared either according to IAS/IFRS using US-GAAP for the treatment of insurance contracts or according to the rules of US-GAAP or according to the rules of the EU-accounting directive. The VVO does not see who should decide which changes will make the financial statements more relevant and reliable to the decision-making needs of users.

To paragraph 35: Redesignation of Financial Assets (Question 5b)

As already stated in the comments to paragraph 3 the VVO has severe objections to a principle which allows a fair value measurement for a great majority of investments with all unrealised gains and losses recognised in the income statement. In the opinion of the VVO such a change of the accounting policy regarding the measurement of insurance liabilities and the related investments should not be allowed in the transition phase until the final standard is in place. The VVO opinion is based on its conviction that the fair value measurement of liabilities arising from insurance contracts and the recognition of unrealised gains and losses resulting from investments in the income statement cannot be considered as an improvement of the information to the users of financial statements.

To paragraphs 7 and 8: Unbundling of deposit components (Question 6)

In order to prevent misunderstandings the VVO points out that the rules laid down in paragraph 6 (Unbundling) of the ED 5 especially apply to the methods of accounting between insurer and reinsurer regarding financial reinsurance. There is no doubt that in case of such contracts it must be clearly distinguished whether premium- and loss-payments for both parties are an income/cost-item or whether they are netted-off in the following periods by opposed cash flows and therefore have to be presented as receivables and liabilities rather than as expense and income. For certain reinsurance contracts it is not easy to assess to what extent a guaranteed reflow of benefits paid by the reinsurer will take place in the following years. If such a reflow is probable, but not guaranteed, the worsening in the reinsurance conditions in the following years, which are the result of high benefits for the ceding insurer in the current year, have to be taken into account in the calculation of a provision for premium deficiency and unexpired risk (which has to be recognised net of reinsurance).[4]

The splitting of payments between the policyholder and the insurer for insurance contracts, where the policyholder bears the insurance risk into payments of premiums and losses and into deposits and the repayment of deposits (as required in the US-GAAP, FAS 97), is not covered by paragraph 7 of ED 5. The separate treatment of the deposit payment in these contracts has no consequence on the result and the disclosure of receivables, liabilities and equity; the only consequence of the treatment in the accounts is, whether the payments of the policyholder and the payments of the insurer at termination of the contract are accounted for in the income statement as income or expenses or directly shown in the balance sheet as increase or decrease of the insurance liabilities.

To paragraphs 18 and 19: Accounting by a cedant for reinsurance (Question 7)

The VVO proposes to include the regulations for financial reinsurance already in phase I of the project. It would be a matter of clarification, which does not result in a change of existing accounting principles.

The VVO proposes to eliminate other regulations in paragraph 18 from ED 5 in phase I. They are drafted in a way, which does not allow to judge whether the drafters correctly did understand the character of reinsurance. The sale of insurance liabilities to another insurance company is not the core reinsurance business; a reinsurance contract normally transfers part of the future risks of the ceding insurer to the reinsurer, which is easier to explain in case of proportional reinsurance than in case of non-proportional reinsurance.

If the insurance liabilities of the ceding insurer are not measured at fair value, the expected future results deriving from a reinsurance contract have to be taken into account only when calculating a provision for premium deficiency and unexpired risk.

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4 Example: in a long duration reinsurance-contract, which can not be cancelled by the ceding insurance company, the reinsurance-commission in the following years is heavily reduced in the case of an adverse result for the reinsurer; therefore the reinsurance net-premium (after deduction of the reinsurance-commission) increases and the result for the reinsurer improves (deterioration for the cedant) in the following years without a guaranteed payment at the end of the contract equalising the open balance between the premiums and the loss-payments at the reinsurers side.

Reinsurance contracts in force may therefore either lead to an increase or a decrease of a provision for premium deficiency and unexpired risk since such provisions have to be calculated net of reinsurance.

To paragraphs 20 to 23: Insurance Contracts acquired in a Business Combination (Question 8)

In the paragraphs 20 to 23 of ED 5 is stipulated that in case of acquisition of an insurance company the insurance liabilities have not to be measured at fair value but according to the measurement principles of the acquirer and the difference between the fair value and the book value of the insurance liability has to be recognized as an asset (Present Value of Insurance in Force- PVIF). The rules of IAS 36 (Impairment of assets) and IAS 38 (Intangible assets) are not applicable to the subsequent measurement of such assets. The measurement of the PVIF has to be carried out in connection with the measurement of the liabilities arising from the related insurance contracts. This means that when determining the need for the establishment of a contingent loss provision both items (PVIF and related insurance liabilities) have to be taken into account.

In the opinion of the VVO the conclusion made in paragraph BC 93, that the asset represents the discounted value of the acquired insurance in force and is only valid for life insurance contracts for which a life insurance provision is set up, is not correct. This question also arises for other types of insurance contracts; it refers – for example – to an insurer, who measures the provisions for unsettled claims on an undiscounted basis and acquires another insurer and in the calculation of the acquisition price the provisions for the unsettled claims of the acquired insurer are measured on a discounted basis. Therefore a clarification should be made, that the principles of paragraphs 20 to 23 are also valid for these cases.

In the opinion of the VVO the rule of paragraph 20 should also be applied to the expectations of renewals and repeat business, which are part of the purchase price for a block of insurance contracts because usually a distinction between expected future profits out of existing contracts and out of follow-up contracts is not made, when an insurance portfolio is purchased. Otherwise this part of the purchase price would be part of the goodwill, a consequence which would not make sense.

The VVO believes that

- acquired insurance liabilities should be compulsory measured using the principles of the acquirer, since a different measurement for different portions of the insurance in force does not make any sense.
- the value of the insurance in force (the expected future benefits arising from the acquired contracts), considered in the determination of the purchase price of an investment in an insurance company, has to be recognised as a separate asset item in the consolidated financial statement. The asset represents the expected future surplus arising from the insurance contracts of the acquired company, taking into account the measurement of the insurance liabilities in the balance sheet of the acquiring insurer[5]. Thereby not only the expected future benefits arising from the existing contracts, but also the expected benefits resulting from follow-up contracts with the policyholders of the acquired company are taken into account. The expected benefits arising from the acquired insurance in force and those from follow-up contracts are often not separated in the calculation of the purchase price; therefore it would be not make sense to treat these two components of the purchase price of the acquired insurance in force differently, even if the same treatment might not be consistent with other IAS principles.
- the asset "Present Value of Insurance in Force", has to be amortised according to the realised benefits. In addition the carrying amount of the asset has to be taken into consideration in a loss recognition test.

The VVO agrees to the regulation in paragraph 21 that the same procedure shall be applied if a block of insurance contracts is purchased. It has to be mentioned that usually a distinction between future benefits out of existing contracts and out of follow-up contracts is not made when an insurance portfolio is purchased.

In most cases the price for the acquired insurance portfolio can be derived from the documents relating to the determination of the purchase price for an investment in another insurance company. In the opinion of the VVO the fair value of the insurance liabilities

5 The carrying amount of the asset differs from the value of the insurance in force considered in the calculation of the purchase price of the investment in an insurance company if the insurance liabilities are measured in another way by the acquiring insurer than by the acquired insurer.

related to the acquired portfolio can nevertheless not be derived from the acquisition price since the latter is highly influenced by the individual interests of the acquiring and selling party.

Paragraph 24: Discretionary participation features in insurance contracts (Question 9)

A discretionary participation feature is the right of the policyholders laid down in the insurance contract or in the statutes of the insurance company to participate in the surplus of the insurer. These features usually leave a certain degree of liberty regarding the amount and timing of the participation to be allocated to the policyholders.

In ED 5 there are no principles for phase I to what extent such rights of the policyholder should be presented as liability item in the balance sheet. There is only the regulation to allocate them either to equity or to liabilities; this means, that it is not permitted to set up a balance sheet item "Not yet allocated surplus". More specific regulation on the discretionary participation features shall be set up in phase II.

The Board has taken the decision that in phase I no accounting guidelines for discretionary participation features are given, with the exception of the prohibition to recognise a balance sheet item "Not yet allocated surplus". It has to be mentioned that in cases, where the contractual right of the policyholder is to participate in the realised surplus, problems arise if the reported surplus contains unrealised gains and losses. The IASB should at the latest for phase II clarify that the rights of the policyholders to participate in the profit of the insurers are constructive obligations – even if the participation is not contractually based but granted due to competition reasons – and that these obligations must be recognised as liabilities in the financial statement.

There may come up the question on how to proceed, if contracts qualifying as financial contracts contain a participation feature. Paragraph 25 requires to treat such contracts in analogy to insurance contracts and that this may mean to account for payments of the policyholders as premium payments, if this is consistent with the accounting principles in force. This procedure is contradictory to the principles valid for other financial contracts.

The VVO is highly interested on how the treatment of the discretionary participation features is resolved in the IFRS-I as in Austria the majority of the whole life, endowment and annuity insurance contracts contain such features, providing a participation of 85 % to 95 % of the surplus. In the course of the preparation of the financial statement of an insurance company the board of directors decides on the level of policyholder participation. This part of the surplus is recognised as a liability in the balance sheet, even if the actual allocation is carried out at a later date. Such a presentation is necessary as the allocation of parts of the surplus to the policyholder creates a liability, not towards the single policyholder (which is given in the moment of the individual allocation), but towards the collective of policyholders.

ED 5 creates an additional problem if the surplus of the company contains unrealised gains from investments and the board of directors can not decide on the participation level for these amounts at the time of the preparation of the financial statement as the claim of the policyholder is derived from the reported surplus in the financial statement, which does not contain unrealised gains.

In financial statements, which are prepared in accordance with the IFRS-I a liability for deferred policyholder claims for not yet realised gains has to be set up, similarly to deferred tax liabilities arising from temporary differences between the book value and the tax value of assets and liabilities. Such deferred rights of the policyholders can change – in contrary to rights which arise from realised surpluses – in the following years, if unrealised gains are reduced in the following years or are compensated by other losses.

The VVO does not agree to permit insurance companies to retain the existing treatment of discretionary participation features and to permit the disclosure within equity, if parts of the unallocated surplus are payable to the policyholders. It should already be prescribed in phase I, to account for these parts of the surplus, which have to be assigned for legal or constructive reasons to the policyholders, as liability. It may be indicated that the principles for deferred tax can or shall be used correspondingly.

To paragraph 30: Disclosure of the fair value of insurance assets and insurance liabilities (Question 10)

The ED 5 requires beginning with December 31, 2006 the disclosure of fair values of insurance assets (whereby it is not evident whether these assets include receivables from policyholders, agents and other insurance companies or the ceded part of the gross insurance liabilities) and liabilities arising from insurance contracts. Although so far it is not clear which method has to be used to measure insurance liabilities in the financial statements, the IASB justifies its demand to disclose fair values in the notes with the fact that fair values of insurance liabilities and assets will certainly have to be disclosed in phase II regardless which method will have to be used to measure insurance liabilities and assets in the balance sheet in phase II.

The VVO objects to the disclosure of fair values in the notes, as long it is not clear how the insurance liabilities have to be measured in the financial statements in phase II and how the fair values have to be computed. Instead, the VVO proposes to disclose the assumptions and methods used to measure insurance assets and liabilities in the balance sheet.

In addition the value of the portfolio of the life insurance contracts may be disclosed in the notes since the law of big numbers makes the technical risk (mortality and survival) of life insurance contracts better calculable and predictable than the technical risk resulting from other insurance contracts.

The notes may contain the expected value of the life insurance portfolio, calculated on the basis of assumptions on biometric risks, on future investment returns and on surrenders; alternative values, based on other assumptions (sensitivity analysis) may be disclosed additionally. These disclosures can provide useful additional information for the users of annual accounts. It should be mentioned, that the value of the portfolio disclosed in the notes is highly dependent on the measurement of the liabilities of the insurance contracts. The lower the measurement of such liabilities, the lower is the value of the portfolio not recognized in the balance sheet.

To paragraph 26 to 29: Other disclosures (Question 11)

In addition to the disclosure of fair values of assets and liabilities resulting from insurance contracts ED 5 requires the disclosure of the

a) explanation of reported amounts and

b) information enabling the user to understand the estimated amount, timing and uncertainty of cash flows.

In principle the VVO agrees with a part of the proposed disclosures provided that the balance between qualitative and quantitative informations makes sense. It must be indicated, however, that various disclosure requirements would lead to undue cost and effort for insurance entities, if the requirements in the implementation guidance have to be fulfilled.

Regarding the disclosures required in the IG the VVO questions why no schemes are determined for the format of the balance sheet and profit and loss accounts, in order to enhance comparison of the financial statements internationally. Beside the obviously ideological reasons of the IASB against the use of prescribed formats, there is no reasonable justification to deny the use of a prescribed format[6], (they have been successfully used in the European Union for decades), which could be flexible in a way by e.g. allowing not to disclose separately immaterial items. It would be necessary to decide which items shall be disclosed as line items on the face of the balance sheet and the profit and loss account and which items need further disclosure of details in the notes.

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6 The reasons given in BC 124 for not regulating in the standard a format and for not defining certain items in the notes are not at all convincing the VVO.

The VVO believes that the disclosure requirements should not oblige insurance companies to disclose internal information exceeding the disclosure requirements for other industries. Regarding details of the company/group policy, which may influence the competitive position of the reporting enterprise in a negative way, confidentiality must be granted. Furthermore and without giving details at this place of the Position Paper the VVO stresses, that parts of the disclosure requirements provided in ED 5 and IG do not lead to useful information for the users, since the information would be either a verbal description of issues dealt in textbooks for management of insurance enterprises (e.g. indicating, that before an insurance contract is issued a risk check is carried out or indicating that the loss ratios of the individual contracts are monitored, or that contracts with high loss ratios should be cancelled) or the disclosure of figures which do not give any useful information or allow any meaningful conclusion by the user (e.g. insured sums of the insured risks). Disclosing "prefabricated" text-components or amounts will introduce further hurdles for the user to receive relevant information.

Detailed comments to the detailed descriptions of the required disclosures in the Interpretation Guidance are given in Section 2 of the Position Paper.

To paragraph 4, subparagraph e: (Question 12)

The ED 5 requires that guarantees given in connection with the transfer of an asset or a liability, should be treated as financial instruments according to IAS 39. Paragraph BC 46 subparagraph c defines that for contracts, which qualify as insurance contracts under paragraph BC 46, subparagraph b, it is necessary at inception of the contract to review the necessity to set up a provision for premium deficiency and unexpired risks.

The VVO agrees to the planned distinction between guarantees, which are financial instruments in accordance with IAS 39, and guarantees from insurance companies covering the risk of non-payment (of receivables).

Additional comments

Deferred acquisition costs

In the opinion of the VVO deferred acquisition costs for insurance contracts and financial contracts should be treated in a uniform way in phase I. IAS 39 should be changed in such a way to allow for the two contract-types in phase II, supposing their consistency with contracts in terms of IAS 18 (Revenue recognition), a deferral of the acquisition costs, even for internal costs like commissions paid to employees. However, the deferral should be limited to acquisition costs which are directly attributable. The depreciation of these deferral items should be effected within the timeframe of recognition of revenue from the related contracts.

Section 2: Comments to the Draft Implementation Guidance Issues

Comments to the details on Disclosure Requirements

IG 7:

(a) up to (d), (h), (i), (j)

Since insurance enterprises will be allowed to use during phase I accounting methods which they are already applying, it is necessary to explain in the notes how various items of the financial statements are composed.

The Austrian Insurance Association (VVO) suggests, however, that for phase II in the IFRS or in an IG to the IFRS a definition of the contents of the following line items and of the following principles of accounting should be given in order to make financial statements of different enterprises comparable:

– definition of premiums written

– definition of earned premiums

– definition of acquisition costs

- definition of claims paid
- definition of claims incurred
- definition of claims handling costs
- treatment and disclosure of revenues and debtors arising out of salvage sold and of subrogation
- permission to recognise the result from inward reinsurance in the financial year following the reinsurance accounting period
- treatment of co-insurance and pool agreements

Premium deficiencies should not be included in the claims incurred; they should be taken into consideration in the calculation of provisions for premium deficiency or unexpired risk.

To the remaining subparagraphs of IG 7 the VVO gives the following comments:

(e)

Information which might be of relevance for users of the financial statements shall consist of narrative details regarding the degree of prudence used to set up financial statements.

(f)

Regarding the treatment of embedded options and guarantees ED 5 and the related IG contain sufficient guidelines. The restatement in the notes should therefore not be obligatory unless there exist particular circumstances.

(g)

In the notes it should be stated how the profit participation of policyholders is treated in the financial statements. It should also be stated, how the premiums received for contracts where the investment risk is borne by policyholders and the benefits paid to policyholders based on the before mentioned premiums are treated in the financial statements.

(k)

Every user of the financial statements of an insurance enterprise should be familiar with the fact, that the accounting principles for financial investments and insurance liabilities have the most significant effect on the amounts included in the financial statements. Such a statement in the notes should therefore not be obligatory unless there exist particular circumstances.

IG 8:

The VVO rejects the idea of measuring the insurance liabilities at fair value, if this leads to a recognition of non-realised profits. In any case the disclosure of such a value should not be required as long as its calculation in phase II of the IFRS is not regulated.

In principle the VVO has no objections against the disclosure of the embedded value of the life-insurance portfolio in the notes. The value of the life-insurance portfolio is primarily depending on the estimated future earnings from financial investments; if the embedded value of the portfolio has to be disclosed in the notes, all other assumptions used for the computation of this value (mortality, future profits of investments and lapses) should also be disclosed. It may also be useful to indicate the changes of the value of a life-insurance portfolio, if the mortality, the future profits from investments and the lapses, compared with the assumptions made, vary within the range of certain percentage points. In the case of life insurance with profit-participation of the policyholders, the impact of the profit-participation on the value of the life-insurance portfolio has to be stated.

It should be mentioned, that the amount stated as embedded value of the life-insurance portfolio in the notes depends on the assumptions made in the measurement of the insurance liabilities set up in the balance sheet.

IG 9:

In the opinion of the VVO the comparability of the financial statements of insurance enterprises – which is one of the major goals of the international accounting standards – can only be achieved, if a minimum layout for the balance sheet and for the income statement and, if necessary, for the cash-flow-statement is mandatory.

IG 10 up to IG 13:

In the opinion of the VVO the disclosure of the following items in a fixed sequence on the face of the balance sheet is necessary, if the balance sheets of insurance companies shall be made comparable:

Assets:

a) Participating interests in other companies

b) Other investments and deposits with ceding insurance companies

- Interest-bearing securities and loans with fixed amounts and dates for repayment
- Interest-bearing securities and loans, where the interest and repayment depends from the results of the debtor
- Interest-bearing securities and loans, where the interest and repayment is influenced by a variable (embedded derivative)
- Loans on policies
- Participations in investment funds
- Shares and other securities, entitling the holder to participate in the surplus and the equity of the issuer, and other participating interests
- Profit-sharing rights
- Real estate (land and buildings)
- Deposits with banks
- Other financial investments
- Deposits with ceding insurance companies

c) Reinsurance assets related to gross insurance liabilities

d) Debtors arising out of direct insurance operations

- Policyholders and intermediaries
- Insurance companies

e) Debtors arising out of reinsurance operations

f) Tangible and intangible fixed assets

– Tangible fixed assets (other than real estate)
– Intangible fixed assets

g) Deferred acquisition costs

h) Other assets

– Cash at bank, cheques and cash in hand
– Miscellaneous debtors
– Prepayments and accrued income
– Miscellaneous assets

Liabilities and stockholder's equity:

a) Equity

– Paid-up capital
– Reserves
– Non-realised changes in the value of the financial investments disclosed as equity
– Other equity instruments
– Retained earnings/accumulated deficit

b) Technical provisions (insurance liabilities) and deposits received from reinsurers

– Life assurance (actuarial) provision
– Unearned premiums
– Provision for claims outstanding
– Provisions for bonuses and rebates
– Provision for profit participation of policyholders
– Provision for premium deficiency and unexpired risks
– Other technical provisions
– Deposits received from reinsurers

c) Liabilities arising from direct insurance operations

– Policyholders and intermediaries
– Insurance companies

d) Liabilities arising from reinsurance operations

e) Other provisions and liabilities

- Long term provisions for the claims of employees
- Other provisions
- Subordinated liabilities
- Financial liabilities
- Miscellaneous liabilities
- Deferred acquisition costs
- Other accruals and deferred income

The notes should at least contain the following details or breakdowns to line items of the balance sheet:

- Participating interests:
  - indication of shares in affiliated companies and other participating interests.
- Interest-bearing securities and loans:
  - indication of securities issued by, and loans to affiliated companies and
  - indication of securities issued by, and loans to companies linked to an insurance enterprise by virtue of a participating interest
- Interest-bearing securities and loans, where the amount of interest and repayment is influenced by embedded derivatives:
  - explanation of the main items.
- Participations in investment funds:
  - breakdown in participations in investment funds open to the public and in special funds.

    The carrying amount of the participations in investment funds open to the public should be broken down in funds which predominantly contain shares or bonds; the carrying amount of participations in special funds should be broken down according to categories of financial investments shown in the balance sheet.
- Profit-sharing rights:
  - it should be specified – if such an item is significant – how far there is a risk of financial losses connected with such rights.

– Real estate:

  - indication of the carrying amount of land and buildings which are used by the insurance enterprise itself or by an affiliated enterprise for operative purposes.

– Intangible assets:

  - indication of the carrying amount of purchased insurance portfolios.

– Reinsurance assets related to gross insurance liabilities:

  - breakdown according to the line items of the technical provisions.

– Miscellaneous receivables, prepayments and accrued income:

  - indication of deferred taxes.

– Retained earnings/accumulated deficit:

  - indication of profit or loss brought forward.

– Provisions for claims outstanding:

  - indication of provisions for incurred but not reported claims (IBNR) and of provisions for claims handling costs.

– Provisions for profit participation of policyholders:

  - indication of the amount remaining after the distribution of profits to the individual policyholders in the course of the completion of the financial statements (amounts available for future distribution).

– Other provisions:

  - indication of provision for deferred taxes.

The total sum of assets and liabilities should be broken down in the notes by currencies, showing those currencies separately, which represent more than one percent of the balance sheet total.

Other breakdowns of investments can be made in domestic and foreign assets.

The VVO would prefer the open deduction of the reinsurance amounts from the gross technical provisions on the liabilities side of the balance sheet instead of disclosing them as assets, as this approach inflates the balance sheet total and is usually corrected when making an analysis of the balance sheet.

IG 14:

In the opinion of the VVO the income statements of insurance enterprises should contain at least the following line items separately:

– Gross earned premiums
– Gross claims incurred and gross expenses for bonuses and rebates
– Gross change in the life assurance (actuarial) provision
– Gross operating expenses
– Gross other technical income and charges
– Realised financial results
– Not realised financial results (as far as they are shown in the income statement)
– Gross other non-technical income and charges

– **Subtotal: Gross result before deduction of the profit participation of policyholders and extraordinary income and taxes**
– Result of the reinsurance ceded

– **Subtotal: Result net of reinsurance before deduction of the profit participation of policyholders and extraordinary income and charges**
– Profit participation of policyholders
– Extraordinary income and charges

– **Subtotal: Profit or loss before taxes**
– Income taxes
– Transfer of non realised financial results (as far as they are shown in the income statement) to a special item in equity

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– **Subtotal: Profit or loss for the financial year (before changes in reserves)**
– Changes in reserves

– **Profit or loss for the financial year shown in the balance sheet**

The notes should at least contain the following details and breakdowns to line items of the income statement:

- Technical income and charges:
  - breakdown in direct and indirect business and in life and non-life business
- Premiums for life insurance:
  - breakdown in current premiums and single premiums and
  - indication of depository payments of policyholders for insurance contracts, where the investment risk is borne by policyholders (if they are included in the premiums).
- Premiums for non-life insurance:
  - breakdown in classes of insurance
- Claims incurred in life insurance:
  - indication of the expenses for redemptions of insurance contracts, for profit participation of policyholders and of repayments of deposits of policyholders for insurance contracts, where the risk of investment is borne by policyholders (if they are included in the claim expenses) and
  - breakdown in capital expenses caused by death, by maturity of contracts, by surrenders and in payments of annuities and a further breakdown in guaranteed benefits and benefits arising from profit participation.
- Claims incurred in non-life insurance:
  - indication of the expenses for bonuses and rebates included in this item and
  - breakdown in classes of insurance.
- Operating expenses:
  - breakdown in acquisition costs (expenses in the reporting year and changes in the deferred expenses if applicable), claims handling costs and other insurance operating expenses.
- Breakdown of the realised financial results:
  - current income (with separated indication of income from real estate)
  - gains from the realisation of investments
  - other financial income
  - investment management charges

- losses from the realisation of investments
- depreciation of land and buildings
- interest charges (excluding interest charges for deposits received from reinsurers) and other charges arising out of investments.

– Breakdown of the not realised financial results:

- non realised increases in value of financial investments
- non realised reductions in value of financial investments

– Breakdown of the result of reinsurance ceded:

- outward reinsurance premiums
- reinsurer's share of claims incurred and of expenses for bonuses and rebates
- contributions of the reinsurers to the operating expenses
- interest yields of the reinsurers for retained deposits
- other income and charges arising out of reinsurance ceded

A further breakdown of these items should be made for reinsurance ceded arising from direct and indirect insurance operations and for reinsurance ceded arising from life insurance and non-life insurance.

IG 15:

The disclosures recommended by the VVO for IG 14 cover widely the disclosures required by IG 15.

Revenues arising from the rendering of services not connected with insurance contracts should be included in the other non-technical income or charges. If they are significant, they should be explained in the notes.

The receipts of payments from policyholders, who bear the financial investment risk, and the repayments to these policyholders, which are not recognised as revenues or expenses in the income statement should be disclosed in the notes.

The VVO points out, that the models of presentation of results mentioned in IG 15 cannot be used alternatively. The model shown in subparagraph (a) is used for property and casualty insurance, the model shown in subparagraph (b) is used for life insurance, especially for the whole life, the endowment and the annuity insurance, and the model shown in subparagraph (c) is used for insurance, where the financial investment risk is borne by the policyholders.

IG 16:

(b)

The effects of changes in estimates and assumptions are constantly and regularly observed by insurance enterprises when ascertaining the run-off results of the provision for claims outstanding; these results are disclosed in the claims development table, required by IG 48 and 49.

Other changes in estimates and assumptions used in the measurement of the insurance liabilities should not occur regularly, but only in particular circumstances. If this is the case (for example a change of the used mortality-tables or a change of the discount rate) the effect should be disclosed.

(c)

The VVO suggests to indicate only the effect of a change of the discount rate.

(d)

The details required in subparagraph (d) can be taken from the proposed items in the layout of the income statement (suggestions to IG 14) and the proposed supplementary disclosures in the notes.

IG 17:

This requirement has been considered in the proposed layout of the income statement.

IG 18:

In principle there is no objection to give the information required by IG 18. The separate disclosure of details should, however, only be required for amounts higher than at least 5% of the total amount.

IG 19:

The required descriptions should be restricted to

– the assumptions used in the calculation of the actuarial provisions for life assurance and (if applicable) for health insurance (discount rates, tables for mortality and for health care costs, assumptions about lapses)
– explanations to deferred acquisition costs (if applicable)
– the calculation of unearned premiums
– the discounting of claims outstanding (if applicable)
– the method of calculation of the provision for premium deficiency and unexpired risk and
– the treatment of non-realised changes in the value of financial investments.

In the opinion of the VVO an explanation of the procedure how to arrive to the assumptions is not useful for the users of financial statements and should therefore not be required.

IG 20:

(a) and (b)

When describing the assumptions used for the calculation of the life assurance actuarial provision the degree of prudence may be pointed out. The mortality tables are normally based on external data, the tables for health care costs are usually based on a combination of internal and external data. The assumptions about lapses are mostly based on internal data; the same applies for the assumptions used for the calculation of a provision for premium deficiency and unexpired risk.

(c), (d) and (f)

In the opinion of the VVO more details about the explanations required in the subparagraphs (c), (d) and (f) should be given by IASB.

(e)

Assumptions about future trends of mortality and health care costs are generally included in the adequate tables; these tables are usually updated only after longer time-periods. Since legal disputes in connection with the settlement of claims cause uncertainties about the amount needed to settle the claim it would bring little improvement for the estimation of the provision if future trends of litigation awards are taken into consideration.

(g)

Uncertainties relating to the share of the policyholders and the shareholders in the unallocated surplus resulting from insurance contracts with discretionary participation features for policyholders should only occur, if the financial statements contain non-realised changes in the value of financial investments, which cannot yet be definitely allocated to policyholders and shareholders. If such uncertainties exist, they should be disclosed and explained in the notes.

(h)

In the opinion of the VVO the disclosures required in subparagraph (h) are redundant, since a user of the financial statements of an insurance company has to know that the estimated future cash flows of an insurance company are inherently uncertain.

IG 21 up to IG 23:

There are no concrete disclosure requirements in these paragraphs.

IG 24:

In the opinion of VVO the disclosures required in IG 24 are only necessary, if in the calculation of the insurance liabilities (life assurance actuarial provision) a modified discount rate or modified tables for mortality or health care costs are used, or if the procedure for the deferral of acquisition costs or for the calculation of the provision for premium deficiency and unexpired risks is modified. If financial investments are reclassified into categories for which different valuation, recognition and disclosure rules for non-realised changes of value are applied, a disclosure should be taken into consideration.

IG 25:

In the opinion of VVO details required by IG 25 will be suitable only in rare cases:

Changes in assumptions may arise in the life and health insurance from changes of the tables for mortality and health care costs, of the discount rate and of the lapse rates used in the premium calculation and in the calculation of the insurance liabilities. Changes in assumptions can also occur in the calculation of the provisions for premium deficiency and unexpired risks for life and non-life insurance. For non-life insurance the effects of changes of discount rates in the assessment of the provisions for claims outstanding may be disclosed. Interdependences between assumptions normally do not exist. The effects of changes of the assumptions used in the calculation of the carrying amounts of assets and liabilities have to be disclosed in the notes both for gross and for net of reinsurance amounts.

IG 27:

The disclosure of the changes in the insurance liabilities and related items as required by IG 27 are – especially for the separated disclosure of the amounts listed in subparagraphs (b), (c) and (d) – not executable.

In the opinion of the VVO it is possible to disclose separately the following amounts included already in the changes of technical provisions:

- effects of portfolio transfers from and to other insurance enterprises
- effects of foreign exchange translation differences
- effects of derecognition of provisions because of lapse of time and
- effects of changes in the assumptions (see IG 25 and 26).

In addition especially in the non-life insurance, the run-off result of the provision for claims outstanding can be shown in a netted way (difference between run-off profits and run-off losses resulting from the provisions for the individual claims).

It has however to be mentioned, that the disclosure of the run-off result may lead to misinterpretations by the users of financial statements, as in many cases a run-off profit may be interpreted as income relating to other periods. As a rule, new provisions for new outstanding claims also contain safety margins which are in conformity with the principle of prudence according to the rules of the IASB. An effect on the result of the financial year is exercised only by the change of the safety margins contained in the provision for claims outstanding. This amount is however especially in some classes of non-life insurance not even known to the executive board.

IG 28:

It is feasable to disclose the figures according to IG 27 also for the preceding financial year; the disclosure of the figures for earlier periods, however, would be cost-intensive and often even confusing.

IG 29:

The presentation of the movements in deferred acquisition costs according to IG 29 can be made in the notes. It is doubtful, however, whether the users of the financial statements receive significant information about the financial situation of the enterprise. In the opinion of the VVO it should be sufficient to state extraordinary changes of the carrying amount (i.e. reduction resulting from premium deficiencies, changes due to modifications of the assumptions) in the notes.

IG 30:

The notes should disclose the development of the carrying amount for acquired insurance portfolios as well as the development of the carrying amount of other fixed assets. If acquisition costs of portfolios are completely amortised due to regular and exceptional depreciation, they should be derecognised as an outflow.

IG 31:

In the opinion of the VVO the text of IG 31 is only a declarative statement without any concrete obligation for disclosures.

IG 32:

In the opinion of the VVO it would make sense, if the disclosure guidelines would contain concrete regulations for what groups of insurance contracts disclosures should be made, e.g. about premiums written in the financial year and the expected follow-up premiums after the balance sheet date based on the insurance portfolio in force, or about claims incurred. Disclosures of the breakdown should only be made for amounts exceeding a certain percentage of the total volume; the remaining amounts should be included in an item "Other".

As an example the VVO can imagine that a breakdown of the total figures into the following groups of contracts (if the amounts for such a group exceed a certain percentage of the total amount) may make sense:

a) Life Insurance

- mixed whole life and endowment insurance with current premiums
- mixed whole life and endowment insurance without current premiums
- pure mortality risk insurance without capital formation

- annuity insurance in process of accumulation
- annuity insurance in process of disbursement
- life insurance where the financial investment risk is borne by the policyholder

b) Health Insurance

- health insurance without possibility to cancel the contract by the insurance company
- health insurance with possibility to cancel the contract by the insurance company

c) Other Insurances

- motor insurance (subdivided into third party liability and other motor insurances)
- accident insurance
- liability insurance
- legal protection insurance
- fire insurance including business interruption caused by fire
- transport insurance
- credit insurance
- hail insurance
- other property insurances
- other classes of insurance

For all groups or classes of insurance a breakdown of the total figures into amounts arising from direct insurance operations and from inward reinsurance operations should be presented.

Another classification can be made in the following way:

- breakdown of the figures for life insurance into contracts with-profit participation features and without profit participation features
- breakdown of the figures for classes of insurance into single insurance contracts and group insurance contracts or into insurance contracts with certain groups of policyholders (e.g. private persons or business enterprises).

In addition to the breakdown of the figures for insurance contracts the figures for contracts classified as financial instruments should be disclosed.

IG 33:

The segments into which certain amounts of the balance sheet and of the income statement should be broken down are listed in the suggestions to IG 32.

IG 34:

In the opinion of the VVO the text of IG 34 is only a declarative statement without any concrete obligation for disclosures.

IG 35:

An insurance enterprise may comply with the requirements of IG 35 by disclosing additional information (e.g. premiums written in the financial year, expected follow-up premiums based on the insurance portfolio in force, number of contracts) for extremely high-risk types of insurance contracts (e.g. professional liability insurance contracts, property insurance contracts with very high risk exposure, non-proportional inward reinsurance contracts with high risk exposure).

IG 36:

The basic breakdowns according to IG 32 should be made in such a way, that a reconciliation of the figures for the individual groups with the figures of the total business is possible; this is not necessary for additional breakdowns according to IG 35.

IG 37:

In the opinion of the VVO the major parts of the disclosure requirements stated in IG 37 will hardly provide additional information to the users of the financial statements to assess the financial situation and the standing of an insurance enterprise, because parts of required disclosures consist of an enumeration of generally accepted principles of business management of insurance enterprises, which have to be applied by the executive board of each insurance enterprise, and other disclosures give only information about measures taken by the management, the effects of which can be widely variable.

The requirements of disclosures contained in IG 37 and the following paragraphs should be carefully tested:

– if they are of real use to the users of the financial statements
– if the required informations can only be elaborated with high costs so that the cost-usefulness-ratio is bad
– if the required informations are primarily useful to competitions; it cannot be understood, why insurance enterprises should be obliged to disclose more details of their business policy than enterprises in other branches.

(a)

In the opinion of the VVO the disclosures required in subparagraph (a) can only be narrative descriptions because quantified details would not provide useful information for the users of the financial statements, but disclose detailed information about the business policy of the insurance enterprise to the competitors.

(b) and (c)

The judgment given to the disclosures required in subparagraph (a) is also valid for the disclosures required in subparagraphs (b) and (c). For example the amount of retention limits for an insurance class depends on the volume of the portfolio as well as on the structure of the insurance contracts. As the user of the financial statements does not know details of the volume and the structure he cannot make conclusions about the adequacy of the retention limits.

(d)

The VVO understands the disclosures required by subparagraph (d) to give information, whether an enterprise or a group accepts insurance risks which may cause losses, provided that other business connected with these risks brings profits. The VVO thinks that "business combinations" of that kind (e.g. bad risks of an important policyholder with contracts for many good risks are covered by the insurance enterprise) have no essential influence on the result of the enterprise; in the opinion of the VVO a disclosure of this kind of business policy does not make sense. It may however make sense to give information if the result of the financial year is adversely influenced by the development of new products or markets, which should bring profits in the following years.

(e)

In the opinion of the VVO disclosures about the asset and liability management (ALM) are only useful for life insurance with capital formation (whole life, endowment and annuity insurance), where the financial investment risk is borne by the insurance company. For this business area a breakdown of the insurance liabilities and of the expected future premiums arising from the portfolio in force by discount rates, and of the financial investments covering such liabilities by categories (real estate, interest bearing investments, shares), can be useful for the users.

(f)

In the opinion of the VVO the disclosure of agreements entitling the insurance enterprise to receive additional equity capital or committing the insurance enterprise to contribute additional equity capital to other enterprises when specified events occur (i.e. profit and loss sharing agreements between a parent company and affiliated companies) makes sense; the disclosure should, however, be amended by an assessment of the risk, that the title to receive additional equity capital when the specified event (i.e. a huge loss) occurs will be fulfilled by the debtor (committed enterprise or person).

IG 38:

(a)

The description of the nature of the covered risks required by subparagraph (a) should be fulfilled by the breakdown of the premiums and the portfolio of policies into classes of insurance, as proposed in the suggestions to IG 32. A brief summary description of the nature of an annuity insurance, an accident insurance or a fire insurance seems to be superfluous.

(b)

A description of concentrations of insurance risks would go too far, if quantified data should be disclosed. If an insurance company is managed duly, risk concentrations, which are not avoided by the underwriting policy are shifted to reinsurers by appropriate contractual agreements. It might only make sense to disclose - in accordance to subparagraph (b) - inappropriate risk-concentrations, which are not shifted to reinsurers; this should, however, occur only in very rare cases.

(c)

In the opinion of the VVO additional explanation by the IASB of the disclosures required in subparagraph (c) is necessary.

(d)

Comments to subparagraph (d) are given in the statements to IG 48 and 49.

(e)

In the opinion of the VVO the disclosures required by subparagraph (e) can only state, for which part of the insurance liabilities

– a fixed rate of interest is guaranteed to the policyholders

– the interest rate depends on the performance of certain investments or

– the interest rate is subject to the discretion of the insurance enterprise.

From the Austrian point of view it is very improbable that insurance contracts exist in which the rate of the interest credited for the premiums collected is at the discretion of the insurance enterprise.

(f)

It makes sense to describe the profit participation system of the insurance enterprise briefly (indication of the classes of insurance, in which a profit participation of policyholders exists, of the parts of the surplus allocated to the policyholders according to the law or to the contract or to a long lasting practice, and of the principles of allocation to the individual insurance contracts).

IG 39:

(a)

In the opinion of the VVO the breakdown required in subparagraph (a) makes only sense for whole life, endowment and annuity insurance contracts. For whole life and endowment insurance contracts and for annuity insurance contracts in the capital formation phase it can be useful, to break down the life assurance actuarial provision by expiring-dates of the whole life and endowment contracts and by the start of the disbursement-phase for annuity contracts and to state the premiums arising out of the insurance business in force in the years after the balance sheet date; these amounts might be grouped by 5-year-periods. An additional disclosure about the extent of earlier cash-outflows based on death or lapses seems not to be necessary, because future lapses are hard to estimate. In general the disclosure of gross amounts should be sufficient, as reinsurers as a rule do not participate in the financial result; the direct insurer bears the risk resulting from the investments arising out of gross business.

For annuity insurances in the phase of disbursement the life assurance actuarial provision for annuities might be broken down depending to the age of the policyholders (grouped by 5 year-periods with separate amounts for men and women).

(b)

Disclosures according to subparagraph (b) would only make sense, if policyholders receive higher payments in the case of a lapse than the insurance liabilities recognised in the balance sheet. If the insurance business is well managed and insurance liabilities are correctly accounted for, this should not be the case.

(c)

A proposal for the disclosures required in subparagraph (c) is made in the comment to IG 40, subparagraph (d).

(d)

The breakdown required in subparagraph (d) is already foreseen in the additional informations proposed in this Position Paper for IG 10 up to IG 13.

(e)

The disclosures regarding the effects of a change in key assumptions (discount rate, mortality rate, probability of sickness, probability of lapses, loss rates and cost rates) are dealt with in the proposals for the disclosures of data for the sensitivity analysis.

(f) and (g)

There are no objections to publish the rules for guarantee funds and the resulting (existing and potential) obligations of the insurance enterprise in the notes; the same applies for disclosures of rules of segregation in case of bankruptcy for certain assets (rules for guarantee funds to cover life insurance liabilities).

IG 40:

(a)

The purpose of the disclosures required in subparagraph (a) cannot be understood. It is not possible that the entire internal information on insurance risks available for the executive board is published for the user of the financial statements.

(b)

The VVO agrees to disclose information about risk exposures – as far as they are possible and make sense – both for the gross and the net of reinsurance portfolio; the VVO can, however, see no possibility to consider policyholder participation features in the determination of the net-amount of risk exposure.

(c)

A comment to the requirements of subparagraph (c) is not possible until there exists clarity, how quantified information about insurance risks should be designed. The VVO has in any case great doubts, that disclosures, which are helpful for the users of financial statements, can be provided.

(d)

In the opinion of the VVO the disclosure required by subparagraph (d) might be given by breaking down the life assurance actuarial provision and the premiums for whole life, endowment and annuity insurance contracts arising out of the insurance portfolio after the balance sheet date by discount rates, because by disclosing these figures each user of financial statements can recognise and estimate the risk of interest losses (see also the comments to IG 39 subparagraphs (a) and (c)).

Disclosures of the capital at risk resulting from capital life insurances and of the liabilities for annuity insurances, both subdivided by groups of age of the insured persons, would enable the user of the financial statements to assess the mortality risk arising from the life insurance portfolio. A breakdown of the capital at risk net of reinsurance by groups of age would however be difficult.

(e)

In the opinion of the VVO the disclosures required by subparagraph (e) are not necessary.

(f)

The explanation to be given to the users of the financial statements about the inherent uncertainty of all statements on risks required in subparagraph (f) shows, that the claim of the VVO, to reduce those disclosures to a reasonable dimension makes sense; only disclosures which provide useful information to a qualified user of financial statements of insurance companies should be required.

(g)

Sensitivity disclosures about the effect of changes of variables that have material effect on the results and the equity make – in the opinion of the VVO – only sense for the following data:

- for all classes of insurance
  - change of the return of the investments
  - change of the expense ratio

- for life insurance
  - change of life expectancy relevant for the result of capital insurance
  - change of life expectancy relevant for the result of annuity insurance
- for non-life insurance
  - change of loss ratios, broken down by lines of insurance

A comment to the required disclosures of material concentrations of insurance risks needs further explanation what is meant by concentrations to be stated in the notes.

The development of prior year insurance liabilities (apparently in the current year) makes only sense for the provision of claims unsettled (disclosure of the run-off result of the provision); we refer, however, to the comments made to IG 27 on the restriction of the value of this information).

IG 41 up to IG 43:

As already indicated in the comments made to IG 40, the effects of changes of the return of investments, of the cost ratio, of the mortality rate in the life insurance and of the loss ratios in the non-life insurance can be stated without major difficulties. For the loss ratios a reasonable breakdown into groups of classes of insurance should be made, since there exist insurance lines with rather stable loss ratios and other lines with rather volatile loss ratios, which are however mostly reduced significantly by reinsurance ceded. Therefore in some classes of insurance there can be huge differences between the change of the gross loss ratio and the loss ratio net of reinsurance. A forecast how the loss ratios will develop in the future can hardly be made by the users of the financial statements – often even not by the executive board of the insurance enterprise – because these ratios are not only influenced by the extent of the losses incurred but also by changes of premium levels.

Regarding to the effects on results of an insurance enterprise it is necessary to disclose the effects of changes of key assumptions on the profit participation in classes of insurance with profit-participation of policyholders. Furthermore the effects on the results and on the equity are reduced by taxation.

IG 44 up to IG 46:

The VVO is sure, that there exists no insurance enterprise, in which material concentrations of insurance risk are not monitored and controlled. The business policy of an insurance company can be directed either by the mitigation of concentrations of risk by its underwriting policy, or by the transfer of concentrations of risk to other companies by reinsurance contracts or other transfer instruments.

It is difficult to define, what is understood by concentrations of insurance risk. The nature of insurance consists in covering as many as possible similar risks, to find an equalisation of risks by the law of large numbers.

In the opinion of the VVO narrative descriptions of the policy applied by an insurance enterprise to cope with concentrations of insurance risk does not give useful information to the users of financial statements. On the other side a significant quantification of the concentration of risks is impossible, since the problems arising from concentrations of risks vary according to the size of the insurance company, the structure of the policyholders, the underwriting policy and the reinsurance policy.

Referring to the examples given in subparagraphs (c) and (d) it is a fact, that an insurance enterprise is exposed to unexpected changes in trends and changes of the financial markets; these exposures generally cannot be eliminated by reinsurance instruments. To a certain degree it is however possible, to transfer parts of the risks by the instrument of profit participation to policyholders.

In the opinion of the VVO disclosures about concentrations of insurance risks in the notes should be omitted, since general remarks do not provide any new insight for the users of financial statements; on the other hand detailed disclosures, which need to be very extensive if they shall make sense, would give the competitors of an insurance enterprise important information about the applied business policy of the disclosing enterprise.

IG 47:

The VVO cannot see any valuable reason to disclose the historical performance of low-frequency high-severity risks, since the fact, that the insured event for the last time happened 40 years ago, does not allow a conclusion whether the event will occur in 10 or maybe in 100 years or never again in the future.

The comments in IG 47 show, that also the IASB recognises that a period of one year is too short for a correct statement of the result of an insurance enterprise, and that therefore the inclusion of an equalisation item in the balance sheet would make sense. The appropriate calculation of such an equalisation item is, however, confronted with the problem, that each method of calculation based on the volatility of the past leads to wrong conclusions, if the structure of the business of an insurance company has changed significantly in the meantime.

IG 48 and IG 49:

A presentation of the development of the loss ratios in the various classes of insurance for a longer period (i.e. 10 years) shows to the users of the financial statements, to what extent in the prior years variations of loss experience, both for gross and net of reinsurance have occurred. Insights for the future developments of losses are, however, restricted, above all by the fact, that the structure of the insurance portfolio may have changed significantly in the meantime; such uncertainties are growing the more the observation period extends into the past.

In the opinion of the VVO despite of the mentioned constraints, the disclosure of loss ratios for groups or classes of non-life insurance contracts for the last 10 years, both for gross and net of reinsurance can be a reasonable information for the users of financial statements. For life insurance the disclosure of the mortality results of the last 10 years (for whole life and endowment insurances in a percentage of the capital in risk, for annuity insurances in a percentage of the life assurance actuarial provision at the beginning of the business year) may be a beneficial information.

To the presentation of the development of claims of a business year in the following periods required in IG 49, the VVO points out that such analyses of run-off results of provisions for claims outstanding are prepared by insurance enterprises at regular intervals, in order to monitor the plausibility of the provision for claims outstanding in classes of insurance with a low-volatile loss ratio. Analyses of the run-off results are also an important tool for the auditor to assess the adequacy of the provisions for claims outstanding.

For monitoring purposes analyses of run-off results are only suitable, however, if they are prepared separately for individual classes of insurance, and the evaluation is not only based on absolute amounts but also on the percentages of the premiums earned in the business years. The VVO doubts therefore, whether the format of a claims development table shown in IG 49 provides practical information for the users of financial statements, if the table is prepared for the total insurance business. A presentation of the table in the notes broken down by classes of insurance would however – in the opinion of the VVO – exceed a sensible disclosure. In principle, the users of the financial statements should rely on the accuracy of the financial statements prepared by the executive board and checked by the auditor; a plausibility check of the amounts stated in the financial statements by the user should therefore not be necessary.

In addition to the comments given the VVO would point out that in the headings of the columns of figures and in the associated comments it is stated that the insurer makes assumptions regarding the amounts of payments for claims under the insurance contracts of a business year. If the development of the provisions for claims unsettled in subsequent years shall be presented, the input assumptions refer to the provisions for claims occurred in a business year, but not to the claims arising from insurance contracts in force in a business year.

IG 50:

In the opinion of the VVO disclosures about the interest risks should be restricted to guarantees given to the policyholders for insurance liabilities stated in the balance sheet, and for premiums expected after the balance sheet date arising out of insurance contracts in force (see comments to IG 39 subparagraph (a)).

Credit risks can arise from financial investments as well as from receivables from reinsurers and intermediaries. The amounts exposed to a credit risk from the transactions with a reinsurer are composed by the receivables stated in the balance sheet, and the reinsurer's share of insurance liabilities reduced by deposits received from the reinsurer; in measuring the credit risk, third-party guarantees have to be taken into account. In the opinion of the VVO it does not make sense to make disclosures about these risks except for the case that losses resulting from these risks are probable; in this case a provision for these losses should be set up in the financial statement.

In the opinion of the VVO the credit risk resulting from credit insurance contracts is a technical risk like any other insurance risk resulting from insurance contracts.

IG 51:

As explained in the comment to IG 39 subparagraph (b), cancellations of insurance contracts normally do not cause any additional interest risk. Disclosures on reductions of interest risks resulting from terminations of insurance contracts before maturity should not be required compulsory because assumptions about lapse-rates in the future are very uncertain.

IG 52:

In the opinion of the VVO an increase of the interest risk caused by participation features with policyholders is not possible.

A reduction of the interest risk caused by participation features with policyholders is given

– if deficiencies in the returns of investments in business years, in which these returns do not reach the guaranteed interests, can be offset in the subsequent periods against additional returns of investments in the calculation of the profit participation of policyholders
– if in business years, in which deficiencies in the returns of investments occur, gains from other income sources have not to be disbursed to the policyholders because the calculation of the profit participation of policyholders is based on the net surplus of a class of insurance.

The possibility of offsetting deficiencies against additional returns of investments in the subsequent years should be disclosed in the notes. In the opinion of the VVO it is not possible to consider the future possibilities of netting as an asset in the financial statements.

IG 53:

See the comments given to IG 50.

IG 54:

In IG 54 a disclosure of risks from embedded derivatives contained in a host insurance contract is required. These risks are as a rule the same as the risks arising from insurance contracts (interest risk, mortality risk) and commented already in the Position Paper for several times. In the opinion of the VVO additional disclosures of these risks, which are already disclosed in other parts of the notes are not necessary.

IG 55 up to IG 57:

There is no doubt, that the interest risk is a significant risk resulting from life (whole life, endowment and annuity) insurance contracts, if the policyholder receives a guarantee for a relatively high interest rate, and therefore it makes sense to disclose further data in the notes related to this risk.

The mortality risk presented in the example of IG 56, however, is of lower importance. The difference to the mortality risk contained in each life insurance contract consists of the fact, that the capital in risk is not constant, but varies every year due to the value of the investments associated with the insurance contract. If the capital at risk increases, the increase of the mortality risk is in many cases counterbalanced by the fact that a higher portion of the premium can be used for the coverage of this risk and a lower amount is invested in the investment fund of the policyholder; in these cases the mortality risk under such contracts shows no speciality.

IG 58:

It would be necessary to give additional informations about the way in which the disclosures mentioned in IG 58 shall be given. As far as the VVO understands the required disclosures they cannot be fulfilled by insurers.

IG 59:

In the opinion of the VVO the key performance indicators stated in IG 59 give valuable information to the user of financial statements about the performance of an insurance enterprise. Therefore, it would make much more sense to require from all insurance enterprises to disclose comparable key performance indicators instead of the disclosures required in various sections of the IG, which either are at all uncalculable or are of no value for the users of the financial statements.

IG 60 and IG 61:

As already indicated in the comments to IG 8, the VVO rejects for the time being the disclosure of fair value of insurance liabilities in the notes (at least as long as there exist no generally agreed rules for the computation of the fair value).