Chapter 10
Other Assets and Liabilities

10.1 Principles 10.1 and 10.2 propose changes to the measurement of some non-insurance assets and liabilities held by insurers. Under principle 1.1, an insurer is any entity that issues an insurance contract. It would not be reasonable to change the measurement basis for non-insurance assets and liabilities held by an entity for which issuing insurance contracts is a minor activity. Therefore, principles 10.1 and 10.2 apply only to an entity whose primary business is issuing insurance contracts.

10.2 Some consider that principles 10.1 and 10.2 should also apply to a reportable segment (as defined in IAS 14, *Segment Reporting*) whose primary business is issuing insurance contracts. However, this would mean that an entity with one relatively small insurance segement would have to adopt principles 10.1 and 10.2 for all its non-insurance segments as well. Therefore, principles 10.1 and 10.2 apply only if the primary business of the entity is issuing insurance contracts.

Property

Principle 10.1

10.3 An entity whose primary business is issuing insurance contracts should measure its:

(a) investment property using the fair value model in IAS 40, Investment Property; and

(b) owner-ocupied property using the allowed alternative treatment in IAS 16, Property, Plant and Equipment.

10.4 Principle 1.1 proposes that the Standard should deal mainly with insurance contracts and not with other assets and liabilities of an insurer. Some argue that the Standard should not deal with any other assets and liabilities of an insurer, as it would be undesirable for an insurer to account for a transaction in one way, and for a non-insurance entity to account for the same transaction in a different way.

10.5 However, this DSOP proposes that the Standard should deal with two categories of non-financial assets that are particularly important for some some insurers - property, held either as an investment (investment property) or for use in the insurer's own operations (owner-occupied property). This DSOP proposes that some insurers should exercise choices available in IAS 40, Investment Property, and IAS 16, Property, Plant and Equipment, in a way that is broadly consistent with the prospective basis proposed in this DSOP for insurance liabilities and insurance assets and proposed in the JWG draft for financial assets and financial liabilities.

10.6 IAS 39 results in a mixed measurement basis, with fair value measurement for some financial assets and financial liabilities, while other financial assets and most financial

liabilities are measured at amortised cost. Therefore, some consider that it is premature to remove from insurers the cost option that currently exists in IAS 16 and IAS 40.

Investment Property

10.7 IAS 40 permits an entity to choose either:

(a) a fair value model: investment property should be measured at fair value and changes in fair value should be recognised in the income statement; or

(b) a cost model: the cost model is the benchmark treatment in IAS 16, Property, Plant and Equipment: investment property should be measured at depreciated cost (less any accumulated impairment losses). An entity that chooses the cost model should disclose the fair value of its investment property.

10.8 E64 (the Exposure Draft preceding IAS 40) proposed that all investment property should be measured at fair value, with changes in fair value recognised in the income statement. The main argument for this treatment was that rental income and changes in fair value are inextricably linked as integral components of the financial performance of an investment property and measurement at fair value is necessary if that financial performance is to be reported in a meaningful way.

10.9 In finalising IAS 40 in 2000, the IASC Board decided to permit a fair value model for investment property as an evolutionary step forward, but concluded that it was impracticable, at that stage, to require a fair value model. Arguments against a requirement to use the fair value model centred on concerns expressed by some about the reliability of fair value measurements, their relevance for non-financial assets, the resulting volatility in the income statement and the cost of obtaining valuations.

10.10 The IASC Board rejected proposals that:

(a) IAS 40 should cover only investment property held by enterprises that specialise in owning such property (and, perhaps, also other investments) and not cover investment property held by other enterprises. The IASC Board rejected this view because it could find no conceptual and practical way to distinguish rigorously any class of enterprises for which the fair value model would be less or more appropriate; and

(b) IAS 40 should apply only to those enterprises that have a reportable segment whose main activity is investment property. Supporters of an approach linked to reportable segments noted that this approach would require an enterprise to adopt the fair value model when the enterprise considers investment property activities to be an important element of its financial performance and would allow an enterprise to adopt IAS 16 in other cases. The IASC Board rejected such an approach because it would lead to lack of comparability between investment property held in investment property segments and investment property held in other segments.

10.11 For an entity whose primary business is issuing insurance contracts, the majority of its liabilities are insurance liabilities. Under principle 3.1, these will be measured at entity-specific value if IAS 39 is still in place. Under IAS 39, many of its financial assets will be measured at fair value, as discussed in paragraphs 3.59 and 3.60. More consistent financial

reporting will result if such an entity also elects under IAS 40 to use fair value model for its investment property, rather than the cost model.

Owner-occupied Property

10.12 Accounting for owner-occupied property (and for plant and equipment) is covered in IAS 16. IAS 16 requires an entity to measure property, plant and equipment at either depreciated cost (benchmark treatment) or revalued amount less subsequent depreciation (allowed alternative treatment). Under the allowed alternative treatment:

(a) revaluations should be made with sufficient regularity such that the carrying amount does not differ materially from fair value; and

(b) increases in carrying amount above a cost-based measure are recognised directly in equity as revaluation surplus, rather than in the income statement.

10.13 IAS 40 acknowledges that it is sometimes difficult to distinguish investment property from owner-occupied property. Some see this as a reason for treating investment property and owner-occupied property in the same way.

10.14 IAS 40 argues that an investment property generates cash flows largely independently of other assets, whereas owner-occupied property generates cash flows that are attributable not merely to the property, but also to other assets used in the production or supply process. This explains why IASC developed different requirements for investment property and owner-occupied property.

10.15 Some commentators on E64 suggested requiring (or at least permitting) enterprises, particularly financial institutions such as insurers, to use the fair value model for their owner-occupied property. They argued that some financial institutions regard their owner-occupied property as an integral part of their investment portfolio and treat it for management purposes in the same way as property leased to others. In the case of insurers, the property may be held to back policyholder liabilities. However, to ensure that property used for similar purposes is subject to the same accounting treatment, the IASC Board concluded that no class of enterprises should use the fair value model for their owner-occupied property.

10.16 An insurer's plant and equipment will generally be immaterial to its financial statements as a whole. On cost-benefit grounds, therefore, some believe that it is unnecessary to remove the option of applying the IAS 16 cost treatment. However, principle 10.1(b) reflects the view that the allowed alternative treatment in IAS 16 will result in more consistent financial statements for an entity (or reportable segment) whose primary business is issuing insurance contracts.

Deferred Tax

Principle 10.2

10.17 An entity whose primary business is issuing insurance contracts should use discounting in measuring its deferred tax assets and deferred tax liabilities.

10.18 Some argue that it would be undesirable to introduce discounting of deferred tax assets and deferred tax liabilities on a piecemeal basis only for an entity whose primary business is issuing insurance contracts. However, principle 10.2 reflects the view that discounting would result in more consistent financial statements for an entity whose other assets and liabilities are mostly measured as explicit or implicit present values.

10.19 Principle 10.2 does not permit an insurer to measure its insurance-related deferred tax assets and deferred tax liabilities on a discounted basis and its other deferred tax assets and deferred tax liabilities on an undiscounted basis.

10.20 This DSOP does not examine the technical issues that arise in implementing discounting for deferred tax assets and deferred tax liabilities.