

STAFF PAPER

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This paper has been prepared by the staff of the IFRS Foundation for discussion at a public meeting of the IASB and does not represent the views of the IASB or any individual member of the IASB. Comments on the application of IFRSs do not purport to set out acceptable or unacceptable application of IFRSs. Technical decisions are made in public and reported in IASB *Update*.

Purpose of this paper

1. This paper summarises as follows the steps the IASB has taken in developing phase II of its project to develop an insurance contracts standard:
 - (a) Background to Phase II: previous work on insurance contracts
 - (i) Work by the IASC
 - (ii) Phase I of the IASB's project on insurance contracts
 - (b) Phase II
 - (i) Due process documents published
 - (ii) Public hearings and use of consultative groups
 - (iii) Field work
 - (iv) Other outreach
 - (v) Reporting to IFRS Foundation bodies
 - (vi) Effect analysis
 - (c) Compliance with required due process steps
2. This paper accompanies agenda paper 16D *Review draft or re-expose*, which seeks the IASB's view on whether the proposals in its insurance contracts project can be finalised or whether the IASB should re-expose the revised insurance contract standard.
3. We intend to ask the IASB for permission to ballot at a future meeting.

Background to Phase II: previous work on insurance contracts*Work by the IASC*

4. In 1997, the IASC set up a Steering Committee to carry out the initial work on an insurance contracts project.
5. The Steering Committee published an Issues Paper in 1999. The first volume of the Issues Paper analysed the characteristics of different forms of insurance contract and considered the significant accounting issues. The second volume contained 82 illustrative examples, summarised relevant national standards and requirements in 17 countries and summarised the main features of the principal contracts found in eight countries.
6. The Issues Paper attracted 138 responses. The Steering Committee held two meetings of three days each to discuss the comment letters and two further meetings, totalling seven days, to develop a Draft Statement of Principles (DSOP). The Issues Paper indicated the former IASC Steering Committee's intention to publish the DSOP for formal comment. However, when the IASB was formed, the Steering Committee used the draft DSOP¹ as an internal report to the newly constituted IASB. The role of the Steering Committee finished at that point.

Phase I of the IASB's project on insurance contracts

7. The IASB began discussing the project in November 2001, using the DSOP as the initial basis for the discussions. However, the IASB decided not to invite formal comments at that stage on a document that the IASB had not yet discussed, as it takes commentators a great deal of time and effort to develop a response to documents of this kind. Nevertheless, the IASB took the unusual step of making the DSOP available on its Website and this helped to stimulate an active debate, within both the industry and the actuarial community.
8. The IASB split this project into two phases in May 2002. The IASB published its proposals for phase I in July 2003 as ED 5 *Insurance Contracts*. The deadline for comments was 31 October 2003 and the IASB received 133 responses. After reviewing the responses, the IASB issued IFRS 4 in March 2004.

¹ The Draft Statement of Principles was not completed – it did not include the intended chapters on participating contracts and presentation.

9. The IASB consulted its Standards Advisory Council to seek feedback on this project at various times, principally in June 2002, November 2002 and November 2003.
10. The IASB established an Insurance Advisory Committee. The role of the Advisory Committee was to respond to requests from the IASB staff for advice. The Advisory Committee met in April 2002, September 2002 and September 2003 (on each occasion for two days) and the staff consulted it extensively by email, though unavoidably at short notice given the tight timetable for phase I. Between October 2002 and April 2003, the staff sought advice on 17 papers. Members of the committee gave the staff valuable input, although inevitably different members had different views. In view of the quantity and quality of input available from the comment letters on ED 5, the staff consulted the Insurance Advisory Committee less extensively after the close of comments on ED 5.
11. The IASB completed phase I in 2004 by issuing IFRS 4 *Insurance Contracts*, which:
 - (a) Made limited improvements to accounting practices for insurance contracts.
 - (b) Permitted a wide variety of accounting practices for insurance contracts to continue, thus avoiding major changes that phase II might reverse.
 - (c) Required an insurer to disclose information about insurance contracts.

Phase II

12. In mid- 2004 the IASB started work on Phase II. This paper describes the due process and outreach activities on Phase II.

Due process documents published

13. In May 2007, the IASB published a discussion paper *Preliminary Views on Insurance Contracts*, setting out its preliminary view on the main components of an accounting model for an insurer's rights and obligations (ie assets and liabilities) arising from an insurance contract. The IASB received 162 comment letters in response.

14. The IASB published the Exposure Draft *Insurance Contracts* (the ED) in July 2010. The ED had a comment period ending on 30 November 2010. The ED was approved by eleven of the fourteen members of the IASB. 2 members voted against its publication and 1 member abstained from voting in view of his recent appointment to the Board. The IASB received 250² comment letters in response.

Public hearings and use of consultative groups

15. In September 2004, the IASB created a working group to advise it on its project. The working group initially comprised 19 senior executives, analysts, actuaries, auditors and regulators, from 9 countries plus 3 official observers. The Insurance Working Group had six two-day meetings between September 2004 and June 2007.
16. The IASB began its review of the responses to the 2007 discussion paper in February 2008. It decided not to hold public round-table meetings at this stage of the project, noting that the members of its Insurance Working Group would supply input from a wide range of perspectives.
17. The IASB consulted the Insurance Working Group again in April 2008, November 2008 and June 2009, to provide input on a number of issues that followed from the responses to the discussion paper.
18. In December 2010, the IASB held six roundtable meetings in Tokyo, London and Norwalk to listen to the views of, and obtain information from, interested parties about the proposed requirements. The IASB received broad input from 94 participants from 81 organisations in 9 countries, representing a wide variety of constituents (including users, preparers, auditors and others).
19. In addition, the IASB consulted the Insurance Working Group in November 2010, March 2011, May 2011, October 2011 and June 2012 meeting for a total of 6.5 days. At these meetings, the Insurance Working Group considered a total of 58 papers covering all aspects of the proposed IFRS, including: scope, unbundling, recognition, contract boundary, cash flows, discount rate, risk adjustment, residual margin, participating contracts, reinsurance assets, premium allocation approach, disaggregation and volume information, OCI, disclosures and transition.

²Some comment letters have been received in parts. As a result of administrative inconsistencies, some were labelled as sub-parts (eg 2, 2A, 2B, 2C) and others had separate numbers (eg 4 and 114). In total the IASB received 253 letters from 247 respondents

Field work

20. Between October 2001 and June 2002, IASB members and staff conducted field visits to nineteen insurance companies from nine countries. The purpose of these visits was to assess the practical implications of implementing the model proposed in the DSOP (which forms much of the foundation for the model now developed by the Board). The staff and Board members gained a great deal of practical input during these visits.
21. In 2009, the IASB conducted field tests to understand better some aspects of the practical application of the proposed insurance model. Sixteen insurers, based in Asian, Australian, European and North American markets and with life, non-life and reinsurance businesses, participated.
22. Between September 2010 and January 2011, the IASB conducted a further round of field tests, involving 15 insurers, based in Asian, Australian, European and North American markets and with life, non-life and reinsurance businesses. This round was intended to test the proposals in the ED in order to understand how the proposed approach would operate in practice, identify where more detailed implementation guidance may be required, evaluate the costs and benefits of the proposed approach and assess how the proposed approach will help insurers to communicate with users of their financial statements. The IASB and FASB discussed a preliminary field test report at their joint meeting on 1-2 March 2011. The detailed findings of the field test were used by the staff:
 - (a) to better understand the arguments presented to us in our outreach, as well as in the comment letters.
 - (b) in the development of board papers on the specific issues addressed in the testing (eg unbundling, acquisition costs, definition of a portfolio).
23. A high level overview of the responses to the field questionnaire and the IASB's actions on the issues raised is set out in Appendix A.

Other outreach activities

24. The IASB and its staff has, throughout the process, held a large number of meetings³ with individuals and groups of preparers, users, actuaries, auditors, regulators and others in order to test proposals and to understand concerns raised by affected parties. Additionally, IASB members and staff have:
- (a) appeared at many public events to exchange views with constituents.
 - (b) maintained a regular and active dialogue with regulators, standard setters and industry representative groups.
 - (c) obtained the views of users of financial statements through targeted meetings and attendance at user forums in the US, Europe and Asia.
25. At the same time, the IASB staff have used the IASB's website to inform the public about the status of the board's deliberations. In addition to the standard posting of papers, decision summaries and board meeting webcasts, this has included regularly updated material as follows:
- (a) A high level summary of progress on the project, describing the main IASB decisions
 - (b) A high level comparison of the IASB's tentative decisions with the proposals in the ED
 - (c) A detailed summary of the IASB's decisions, that shows how each paragraph in the exposure draft would be affected by the decisions taken each month
 - (d) A 10-15 minute podcast that summarises the insurance contracts meetings for each month and places those decisions in context
 - (e) Topic reports on the IASB's decisions, presented together with working drafts.
26. Interested parties have been notified when these items have been updated using subscriber email alerts. In July 2012, there were over 13,000 subscribers to the insurance contracts email alert.

³ Over 340 meetings since the ED was published.

Reporting to IFRS Foundation bodies

27. IASB members discussed the project specifically with the Advisory Council in November 2007 and October 2011. Education sessions were also held for Advisory Council members in February 2010 and October 2010. In addition, the project was regularly mentioned at the general session on the work plan at each meeting of the Advisory Council.
28. The Due Process Oversight Committee was informed of progress in the project in March 2011, June 2011, July 2011, October 2011 and April 2012. In addition, in January 2012, the Due Process Oversight Committee was informed about correspondence with the HUB Global Insurance Group regarding the accounting for short-duration insurance contracts.

Effect analysis

29. The IASB is committed to assessing and sharing knowledge about the likely costs of implementing proposed new requirements and the likely ongoing associated costs and benefits of each new IFRS—the costs and benefits are collectively referred to as ‘effects’. The IASB gains insight on the likely effects of the proposals for new or revised IFRSs through its formal exposure of proposals and through its fieldwork, analysis and consultations with relevant parties through outreach activities.
30. In evaluating the likely effects of an IFRS for insurance contracts, the IASB has considered the following factors:
 - (a) how the proposed changes are likely to affect how activities are reported in the financial statements of those applying IFRSs.
 - (b) how those changes improve the comparability of financial information between different reporting periods for an individual entity and between different entities in a particular reporting period.
 - (c) how the changes will improve the quality of the financial information and its usefulness in assessing the future cash flows of an entity.
 - (d) the benefit of better economic decision-making as a result of improved financial reporting;

- (e) the likely effect on compliance costs for preparers, both on initial application and on an ongoing basis; and
- (f) how the likely costs of analysis for users (including the costs of extracting data, identifying how the data has been measured and adjusting data for the purposes of including them in, for example, a valuation model) are affected. The IASB takes into account the costs incurred by users of financial statements when information is not available and the comparative advantage that preparers have in developing information when compared with the costs that users would incur to develop surrogate information.

31. Those considerations are described in Appendix B.

Required due process steps

32. Paragraphs 112 and 113 of the IASB's Due Process Handbook state:

112 The following due process steps are mandatory:

- developing and pursuing the IASB's technical agenda
- preparing and issuing IFRSs and publishing exposure drafts, each of which is to include any dissenting opinions
- establishing procedures for reviewing comments made within a reasonable period on documents published for comment
- consulting the Advisory Council on major projects, agenda decisions and work priorities
- publishing bases for conclusions with IFRSs and exposure drafts.

113 Other steps specified in the Constitution are not mandatory. They include:

- publishing a discussion document (eg a discussion paper)

- establishing working groups or other types of specialist advisory groups
- holding public hearings
- undertaking field tests (both in developed countries and in emerging markets).

33. In May 2012, the Trustees of the IFRS Foundation published for public comment an updated version of the IFRS Foundation Due Process Handbook.
34. The revised handbook also presents a reporting template for demonstrating to the DPOC how the IASB has met its due process requirements.⁴
35. This paper demonstrates that the IASB has, for the insurance contracts project, met the requirements of all the mandatory and ‘comply or explain’ due process steps set out in the IASB Due Process Handbook. This paper also demonstrates that the IASB has met the due process requirements set out in the May 2012 draft Handbook as follows:
- (a) Appendix C describes how the IASB has adhered to the protocol for the development of an exposure draft, should the IASB decide to re-expose the proposals.
- (b) Appendix D describes how the IASB has adhered to the protocol for finalisation of an IFRS, should the IASB decide to publish a review draft and finalise an IFRS.

Agenda paper 16D asks the IASB which approach it will take.

Questions for the IASB

Questions

Is the IASB satisfied that that all mandatory due process steps have been met in developing this project?

Are there any further due process steps that the IASB thinks are necessary before proceeding to ballot? If so, what are they?

⁴ Although the appendix accompanies the IFRS Foundation Due Process Handbook, it is not an integral part of the handbook and may be updated from time to time by the IASB and its staff, subject to the approval of the DPOC.

Appendix A: Field tests

- A1. This appendix describes at a high level the responses to the field questionnaire and assesses how the IASB responded to the concerns raised.
- A2. This appendix follows up on Agenda paper 2F/59F *Preliminary report on field tests* for the 1-2 March 2011 meeting, which presented the preliminary results from the field tests of the proposals in the IASB's Exposure Draft *Insurance Contracts*. That paper considered the following aspects of the field tests being performed:
- (c) Population covered
 - (d) Basis of data used by participants
 - (e) Type of feedback received
 - (f) Assumptions and limitations of the tests

That paper was for discussion only and no decisions were requested.

- A3. We note that the field test results are confidential and we are unable to present findings in a way that allows for the identification of any of the results with any particular participant. That said, within these constraints, we have sought to be as transparent as possible in reporting these findings.

Use of information from field test

- A4. In addition to the written reports submitted by field test participants, the staff discussed individual field test results with participants through follow-up meetings and conference calls.
- A5. The specific inputs and supporting material provided by the field test participants were used by the staff:
- (a) To better understand some of the arguments presented to us in our outreach, as well as in the comment letters.
 - (b) To better understand qualitative arguments from respondents on the ED proposals. For example, when the IASB evaluates the merit of the proposals for transition, it may wish to consider information about the

size of the impact in retained earnings of setting a nil residual margin on transition date.

- (c) In the development of board papers on the specific issues addressed in the testing (eg unbundling, acquisition costs, definition of a portfolio).

A6. We note that in general, most field test participants reiterated messages already provided in their respective comments letters or expressed views broadly consistent with views generally expressed in their geographical areas.

A7. The following table provides an overview of the main messages, including a comment on whether the Board addressed the main messages in its deliberations.

Main message	How addressed in redeliberations
<i>Scope and definition</i>	
<p>Definition of a portfolio of insurance contracts - Participants interpreted the notion of ‘portfolio of insurance contracts’ for the purpose of the testing differently, based on different existing local practices or regulatory regimes.</p>	<p>The IASB amended the definition of a portfolio of insurance contracts to ensure greater consistency.</p>
<i>Defining the contract</i>	
<p>Recognition point – Some field test participants indicated that significant changes to systems would be required to identify those contracts which they are bound to, but which have not been entered in the entity’s administration system as yet.</p>	<p>The matter raised by the field test participants was discussed by the IASB. The IASB amended its proposals so that contracts are recognised when coverage begins, with an onerous contract test to be performed during the pre-coverage period.</p>
<p>Unbundling – participants asked for more clarity on when unbundling would be required and how unbundling would be performed. Some questioned the practicality and complexity of unbundling.</p>	<p>The IASB discussed unbundling at length. The IASB clarified and amended when contracts are to be unbundled.</p> <p>Furthermore, the notion of “disaggregation” was introduced so that volume information would be presented in profit or loss in a way that is not distorted by deposit receipts. We believe disaggregation to be less complex than unbundling.</p>
<i>Measurement model: building block 1 – cash flows</i>	
<p>Fulfilment cash flows - Some</p>	<p>The IASB discussed the matters raised</p>

<p>participants considered the wording for calculating cash flows to be too restrictive, as some believed reference to probability-weighted cash flows would automatically point to a stochastic modelling type of technique for the estimate of future cash flows.</p> <p>Furthermore, differences were noted in how direct and indirect costs are currently accounted for.</p>	<p>by the field test participants. The IASB confirmed the objective in calculating the expected cash flows is to determine the statistical mean. The IASB also decided to include application guidance that not all possible scenarios need to be identified and quantified.</p> <p>Furthermore, application guidance will be provided that all direct and directly attributable costs are to be included in estimating expected cash flows.</p>
<p>Acquisition costs - Most participants proposed that acquisition costs included in the fulfilment cash flows should be those which are incremental at a portfolio level.</p>	<p>The IASB discussed the matters raised by the field test participants. The IASB decided to include all direct costs incurred in originating a <i>portfolio</i> of insurance contracts.</p>
<p>Policyholder taxes - Some field test participants considered that fulfilment cash flows should include the amounts of taxes insurers pay in some jurisdictions as a proxy for investment returns being taxed in the hands of the policyholders.</p>	<p>The staff notes that the ED proposed to include in the fulfilment cash flows transaction-based taxes (paragraph B61(h)), and to exclude income tax as defined by IAS 12 (paragraph B62(g)). There may also be other taxes, for which the insurer would apply the principle that the cash flows include all cash flows within the boundary of an existing contract that are incremental at the level of a portfolio of insurance contracts, and no other cash flows. We propose to consider in drafting whether we can clarify the IASB’s intention. We do not intend to discuss this issue with the boards.</p>

<i>Measurement model: building block 2 – time value of money</i>	
<p>Discount rate – it was unclear to some field test participants how exactly to calculate the discount rate.</p> <p>Furthermore, many stated that discount rate changes will introduce significant volatility.</p>	<p>The IASB considered concerns that there is insufficient guidance on how the insurer should determine a discount rate that reflects the characteristics of the liability. In addition, the IASB considered concerns that determining the liquidity adjustment directly can be difficult to do. As a result, the IASB added application guidance on how to determine the discount rate, including that top down and bottom up approaches are both acceptable.</p> <p>The IASB has responded to concerns that the discount rate would introduce significant volatility by deciding that changes in the liability arising from changes in discount rate should be presented in OCI.</p>
<i>Measurement model: building block 3 – risk adjustment</i>	
<p>Risk adjustment – Some field test participants indicated that the risk adjustment and specifically the range of permitted risk adjustment techniques could result in arbitrariness and incomparable results.</p> <p>Furthermore, some field test participants argued that the estimation process to determine risk margins would require significant work and</p>	<p>The IASB discussed the matters raised by the field test participants. The IASB intends to retain an explicit risk adjustment as it would provide more relevant information to users and is believed to be more transparent than is the case under a single margin approach.</p> <p>The IASB also proposes to delete the requirement that the risk adjustment</p>

<p>extensive judgement and that the effort would not always outweigh the benefit.</p>	<p>must be determined using one of three permitted techniques.</p> <p>However, although constituents suggest the exposure draft's proposal to require confidence level disclosures should be removed, the IASB decided to retain that disclosure. In the IASB's view, that disclosure is necessary in order to address concerns about comparability.</p>
<p><i>Measurement model: building block 4 – residual margin</i></p>	
<p>Residual margin – Some field test participants expressed concerns about a locked in residual margin. They argued that, by locking-in the residual margin, an insurer might recognise losses in one period, that will reverse in future periods when the insurer releases the margin. They believe this effect is counterintuitive and will be difficult to explain to users.</p> <p>Furthermore, the release pattern was questioned, because releasing the residual margin on a straight line basis will not necessarily align with the manner in which risk protection and services are provided and with the timing of overhead.</p>	<p>The IASB considered the view that a locked residual margin could lead to counterintuitive effects. Thus, the IASB decided that the residual margin should be unlocked for all changes in cash flows.</p> <p>Furthermore, the manner in which the residual margin is to be released was changed from a straight line basis to a basis that is 'consistent with the manner in which services are delivered'.</p>
<p><i>Premium allocation approach (PAA)</i></p>	
<p>Field test participants raised specific questions on the premium allocation approach, for instance on complexity</p>	<p>The IASB discussed the PAA at length. Concerns by field test participants were addressed as follows:</p>

<p>and about the eligibility criteria.</p>	<ul style="list-style-type: none"> • The premium allocation approach was simplified, for instance, by introducing practical expedients (e.g. not to require discounting in some circumstances) and the requirement that an explicit onerous contract test needs to be performed <i>only</i> when facts and circumstances indicate that the contract is onerous. • The eligibility criteria were clarified and extended so that the PAA can be used when the PAA and the building block approach would produce similar measurement results. (Also, all contracts with a coverage period of 12 months or less qualify for the PAA).
<p><i>Presentation and disclosures</i></p>	
<p>Volatility in profit and loss was a key area of concern because some field test participants believe the ED proposal will not fairly reflect the economics of insurance business. The field test participants suggested dealing with unwanted volatility by revising the proposals on discount rate and presentation.</p>	<p>The IASB considered concerns that there is unwanted volatility. Specifically, volatility was addressed in many different ways, including as part of clarifying the discount rate decision, in considering the use of other comprehensive income and the “mirroring approach” for participating contracts. Some also support unlocking the residual margin, in part because it would reduce volatility.</p>
<p>Presentation – Some field test participants argued that the summarised margin approach requires excessive</p>	<p>The IASB has tentatively decided that insurers should present information about premiums, benefits and claims in</p>

<p>detail about liability movements on the statement of comprehensive income which does not provide useful information.</p>	<p>the statement of comprehensive income, but has not finalised its discussions. Field test participants were not asked to test the ‘earned premium approach’ that the IASB and FASB will consider at a future meeting.</p>
<p>Disclosure - Most field test participants argued that the roll forwards and the reconciliations are burdensome and will result in increased costs for no or minimal benefits. Also, some field test participants considered the requirements to disclose qualitative information about risk exposures and risk management techniques may reveal proprietary information. (The staff notes that this information is currently required by IFRS 4.)</p>	<p>The IASB discussed the matters raised by the field test participants and considered similar comments in the comment letters. The IASB confirmed that an insurer shall aggregate or disaggregate information so that useful information is not obscured by either the inclusion of a large amount of insignificant detail or the aggregation of items that have different characteristics. This is a general principle in IFRSs. Furthermore, the board’s decision on the level of disaggregation is consistent with other projects, such as Revenue Recognition and Leases. We will consider the level of disclosure detail to be required in disclosing roll forward information in a future meeting.</p>
<p><i>Other considerations</i></p>	
<p>Transition - Most field test participants criticised the transition proposal of setting a residual margin equal to zero on date of transition. They indicated that this will not represent faithfully the</p>	<p>The papers for the meeting discuss transition.</p>

<p>profitability of in-force business.</p> <p>Some field test participants suggested other methods of dealing with transition. They for instance mentioned the possibility of retrospective application (though sometimes burdensome) or the inclusion of a margin on transition based on the difference between the result of the measurement under the insurer's existing accounting policies and measurement as per the IFRS.</p>	
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Conclusion

- A8. The staff notes that all the issues raised by the field test participants confirmed the views that were expressed in the comment letters as a whole and which were noted in the comment letter analysis provided to the IASB and FASB in their January 2011 meeting. The staff believe that all the issues raised by field test participants have been adequately reflected in the arguments considered by the boards in the papers relating to those topics. In addition, the staff notes that in most cases, the board's tentative decisions should reduce some of the concerns about the model noted by the field test participants in their reports.

Appendix B: Preliminary effect analysis

- A1. This appendix describes the IASB's considerations of the factors for evaluating the likely effects of an IFRS for insurance contracts.

How the proposed changes are likely to affect how activities are reported in the financial statements of those applying IFRSs.

- A2. At present, insurance contracts are accounted for using the different accounting models that have historically evolved in different jurisdictions and at different times to address the products most prevalent in their jurisdictions. As a result, the proposed IFRS would affect different jurisdictions in different ways. However, one important result of the proposed changes is that all insurers reporting under IFRS would be required to provide relevant and reliable information. This is because we propose to remove the exemption that permits insurers not to apply paragraphs 10-12 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.
- A3. In general, there will be relatively little change for many non-life contracts. The main changes for non-life are:
- (a) The introduction of discounting (and risk adjustment for IASB) in measuring the liability for incurred claims.
 - (b) More information in the financial statements about claims liabilities, changes in risk and effects of discounting.
 - (c) Measuring onerous contracts on an expected claims basis rather than an incurred claims basis.
- A4. For life contracts, there is more significant divergence today and more significant changes would result from the standard. The main changes are:
- (a) Updated assumptions rather than locked-in assumptions.
 - (d) Recognition of guarantees and options previously not recognised (or recognised using a smoothing model) using expected present value of cash flows, discounted using current, market-consistent discount rates.

- (e) More information about assumptions and effects of assumptions including risk and effects of discounting.
- (f) A discount rate that reflects the features of the insurance liability, rather than one that reflects the features of the assets backing that liability. The resulting measurement of the liability will not be reduced by hoped-for investment spreads.
- (g) More transparent information about changes in estimates.
- (h) Cash flows used to determine the margins included in measuring insurance contracts would include acquisition costs. As a result, there would be no need to defer acquisition costs, and no need for complex and hard-to-understand mechanisms for dealing with that deferral.
- (i) One accounting model for all life insurance contracts, rather than different accounting models based on product type.

A5. Accordingly, the proposed IFRS could have a pervasive effect on the financial statements of entities that issue insurance contracts. However, insurance contracts are generally issued by regulated insurance companies, thus the proposed IFRS would affect entities only in one industry.

How the changes improve the comparability of financial information between different reporting periods for an individual entity and between different entities in a particular reporting period.

A6. In considering the likely effects of a new IFRS on insurance contracts, the IASB has placed weight on the fact that, at present, IFRSs have no credible standard on insurance contracts, and that as a result substantial differences occur in the way that different companies account for insurance contracts. The SEC staff paper *An analysis of IFRS in Practice*, published in November 2011, noted that “Of the nine companies in the insurance industry in the analysis, the Staff noted seven different accounting bases used to account for insurance operations. In some cases, companies used a single accounting basis for their consolidated operations, whereas in others, companies used a mixture of accounting bases depending on the subsidiary and type of contract.” An IFRS for insurance contracts would eliminate much of the diversity in practice.

How the changes will improve the quality of the financial information and its usefulness in assessing the future cash flows of an entity.

A7. The proposed IFRS would:

- (a) introduce a comprehensive, coherent framework for the accounting for all types of insurance contract. That framework would reflect the many different ways in which insurers make money whether through fees from asset management services, investment income from spread business or underwriting profit from protection business. An advantage of a comprehensive, coherent framework for all insurance contracts is that, depending on what features are significant to any given contract at any given time, the measurement of the liability reflects those features as appropriate, without creating the cliff effects that would occur if different models were used to reflect the different features.
- (j) measure insurance contracts in a way that uses updated estimates and assumptions, using market-consistent information where available, and that reflects the time value of money and differences in uncertainty relating to the liability. The use of a current value measurement model for the insurance contracts liability is necessary for three important reasons:
 - (i) It provides transparent reporting of changes in the insurance contract liability and provides complete information about changes in estimates.
 - (ii) It results in transparent reporting of the economic value of options and guarantees embedded in insurance contracts.
 - (iii) It means that the assets and liabilities of an insurer are measured on consistent basis, thus reducing accounting mismatch in comprehensive income and equity.

A8. However, volatility is an inevitable consequence of a current measurement model. The IASB has considered concerns that there would be unrepresentative volatility in reported earnings, and many of the decisions it has taken since the ED was published would result in lower volatility than the proposals in the ED. These include providing additional guidance that a 'top-down' approach to determining the discount rate is permitted, requiring the use of other

comprehensive income to present changes in the liability arising from changes in the discount rate, using the residual margin to offset changes in estimates of future cash flows, and the “mirroring approach” for participating contracts.

Benefit of better economic decision-making as a result of improved financial reporting

- A9. The staff believe that users of financial statements would be able to make better economic decisions as a result of the following features of the proposed IFRS:
- (a) It reflects the many different ways in which insurers make money whether through fees from asset management services, investment income from spread business or underwriting profit from protection business.
 - (b) It provides updated information about the insurer’s position, rather than information that reflects the insurer’s expectations when it entered into contracts, possibly decades previously.
- A10. As a result, the staff expect significant benefits would result from improved financial reporting for most jurisdictions.

The likely effect on compliance costs for preparers, both on initial application and on an ongoing basis

- A11. The staff expects significant compliance costs for preparers, both on initial application and on an ongoing basis.
- A12. On initial application, many insurers will need to completely overhaul existing systems in order to obtain the information needed to apply the proposed IFRS. In Europe and jurisdictions that are currently adopting Solvency II requirements for regulatory purposes, entities will be considering an overhaul of existing systems and there may be benefits if entities can implement both financial reporting and regulatory requirements at (or near) the same time. However, that would not be the case in other jurisdictions.
- A13. On an ongoing basis, there would be significant costs associated with actuarial estimation requirements, and with the tracking requirements that would result from the IASB’s decisions on offsetting changes in estimates of future cash flows in the residual margin, on presenting the effect of changes in discount

rates in OCI and on determining earned premium. However, in arriving at its decisions, the IASB has considered those costs and believes that the information produced as a result of those decisions would outweigh the costs of providing it.

How the likely costs of analysis for users are affected

- A14. The effect of the proposed IFRS on the likely costs of analysis for users of financial statements depend on existing practice:
- (a) In general, the proposed IFRS would provide improved information about changes in circumstances, and about the different sources of earnings from insurance contracts. Such information could reduce the cost of analysis by providing information more directly to users of financial statements. However, in most cases, the volatility introduced by a current measurement model means that there is a need for education amongst users of financial statements to help interpret the results applying the proposed IFRS.
 - (b) Where users of financial statements analyse companies from different countries, the problems of diversity in accounting models creates costs which would be alleviated by standardised practice.
 - (c) In the US, where there has been existing US GAAP for insurance contracts for many years, the benefits of the improved information arising from the proposed IFRS needs to be tempered by the loss of trend data and need for education that results from a change in established practice.
36. Where users of financial statements analyse entities in only one jurisdiction, the increase in costs of analysis (eg through loss of trend data and increased training needs) may outweigh the perceived benefits of increased comparability across jurisdictions. However, where users of financial statements analyse entities in more than one IFRS jurisdiction, the benefits of comparability are likely to prevail.

Summary

- A15. In summary, the costs of implementing the proposed IFRS would be extensive for entities that issue insurance contracts. There will be significant loss of trend

data and there may disruption for some years as preparers and users learn how best to interpret the information provided by the new model. However, the benefits of increased comparability between entities and across jurisdictions and more transparent reporting of updated circumstances are expected to exceed those costs on an on-going basis. At present, entities with insurance contracts bear significant costs, partly because users of financial statements find the existing financial reporting opaque, particularly with respect to the risks facing the entity. The expectation is that increased confidence in the financial statements of entities with insurance contracts should provide much needed transparency and lower their cost of capital.

Appendix C: Development and publication of an exposure draft for an IFRS, practice guidance or Conceptual Framework chapter

In agenda paper 16D we discuss whether the proposals in the insurance contracts project can be finalised or whether the IASB should re-expose the revised insurance contract standard. This appendix shows how the IASB has complied with the due process steps that would be required if it were to decide to re-expose the revised insurance contract standard. There is substantial overlap between the due process steps that would be required for a revised exposure draft (set out in this appendix) and for a final standard (set out in Appendix D). We have highlighted in [blue text](#) the rows that are common between this table and Appendix D.

<i>Step</i>	<i>Required/ Optional</i>	<i>Metrics or evidence</i>	<i>Protocol for and evidence provided to DPOC</i>	<i>Actions</i>
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<i>Step</i>	<i>Required/Optional</i>	<i>Metrics or evidence</i>	<i>Protocol for and evidence provided to DPOC</i>	<i>Actions</i>
<p>Board meetings held in public, with papers available for observers. All decisions are made in public session.</p>	<p>Required</p>	<p>Meetings held to discuss topic.</p> <p>Project website contains a full description with up-to-date information on the project.</p> <p>Meeting papers posted in a timely fashion.</p>	<p>Members of the IASB discuss with DPOC progress on major projects, in relation to the due process being conducted, with DPOC.</p> <p>DPOC reviews comments from interested parties on IASB due process as appropriate.</p>	<p>Board meetings</p> <p>The IASB discussed the project at every meeting between December 2010 and July 2012. The IASB also intends to discuss the project at its September and October 2012 meetings.</p> <p>Project website</p> <p>The project website contains a full description with up-to-date information on the project. In addition to the standard posting of papers, decision summaries and board meeting webcasts, this has included regularly updated material as follows:</p> <ul style="list-style-type: none"> • A high level summary of progress on the project, describing the main IASB decisions • A high level comparison of the IASB’s tentative decisions with the proposals in the ED • A detailed summary of the IASB’s decisions, that shows how each paragraph in the exposure draft would be affected by the decisions taken each month. • A 10-15 minute podcast that summarises the insurance contracts meetings for each month and places those decisions in context. • Topic reports on the IASB’s decisions and working drafts. <p>DPOC</p> <p>The Due Process Oversight Committee was informed of progress in the project in March 2011, June 2011, July 2011, October 2011 and April 2012. In addition, in January 2012, the Due Process Oversight Committee was informed about correspondence with the HUB Global Insurance Group regarding the accounting for short-duration insurance contracts.</p>
<p>Formal consultation with the Trustees and the Advisory Council</p>	<p>Required</p>	<p>Discussions with the Advisory Council on topic</p>	<p>DPOC meets with the Advisory Council to understand perspectives of stakeholders on due process of IASB.</p> <p>Advisory Council chair invited to Trustees’ meetings and meetings of DPOC</p>	<p>IASB members discussed the project with the Advisory Council in November 2007 and October 2011. Education sessions were also held for Advisory Council members in February 2010 and October 2010.</p> <p>We intend to report the IASB’s September 2012 discussions on due process to the trustees in October. 2012.</p>

<i>Step</i>	<i>Required/ Optional</i>	<i>Metrics or evidence</i>	<i>Protocol for and evidence provided to DPOC</i>	<i>Actions</i>
Analysis of likely effects of the forthcoming IFRS or major amendment, for example, costs or on-going associated costs.	Required	Publication of effect analysis	Publication of effect analysis	<p>Updates on this project were included in regular reports to the DPOC, and we plan to report a summary of due process at the next trustee meeting.</p> <p>The IASB has paid particular attention to the effect the proposals would have on the volatility of reported results. The IASB plans to include an analysis of likely effects in the Basis for Conclusions to a revised exposure draft, or as a standalone document published with a review draft. A preliminary effects analysis is provided in Appendix B of this paper and the IASB plans to provide a copy of the effect analysis to the DPOC in due course.</p>
Consultative groups utilised, if formed	Optional	<p>Number of consultative group meetings, and evidence of substantive involvement in issues</p> <p>Consultative group review of draft exposure draft</p>	DPOC receives report of consultative group activity from IASB	<p>Since the end of the comment period, the IASB consulted with the Insurance Working Group in November 2010, March 2011, May 2011, October 2011 and June 2012 meeting for a total of 6.5 days. The working group papers covered the all aspects of the proposed IFRS including scope, unbundling, recognition, contract boundary, cash flows, discount rate, risk adjustment, residual margin, participating contracts, reinsurance assets, premium allocation approach, disaggregation and volume information, OCI, disclosures and transition.</p>

<i>Step</i>	<i>Required/Optional</i>	<i>Metrics or evidence</i>	<i>Protocol for and evidence provided to DPOC</i>	<i>Actions</i>
Fieldwork undertaken in analysing proposals	Optional	IASB describes approach taken on fieldwork IASB explains why it does not believe fieldwork is warranted, if that is the preferred path Number of field tests	If fieldwork is deemed by the IASB as not required, DPOC to review and discuss the explanation with IASB DPOC receives a report on field work activities and how findings have been taken into consideration by IASB	The IASB has conducted field work in 2001/2002, in 2009 and in 2010/2011. 2001/2002: field visits to 19 insurance companies from nine countries, to assess the practical implications of implementing the model proposed in the DSOP (on which the proposed IFRS is largely based) 2009: targeted field tests by sixteen insurers, based in Asian, Australian, European and North American markets and with life, non-life and reinsurance businesses, to understand better some aspects of the practical application of the proposed insurance model. 2010/2011: targeted field tests, involving fifteen insurers, based in Asian, Australian, European and North American markets and with life, non-life and reinsurance businesses, to test the proposals in the ED in order to understand how the proposed approach would operate in practice, identify where more detailed implementation guidance may be required, evaluate the costs and benefits of the proposed approach and assess how the proposed approach will help insurers to communicate with users of their financial statements.
Email alerts are issued to registered recipients	Optional	Evidence that alerts have occurred	DPOC receives a report on outreach activities	Interested parties have been notified when updates to the insurance contracts pages are made using subscriber email alerts. At last count there were over 13,000 subscribers to the insurance contracts email alert.
Outreach meetings with a broad range of stakeholders, with special effort for investors	Optional	Number of meetings held and venues documented. Evidence of specific targeted efforts for investors	DPOC receives a report on outreach activities.	IASB members and staff have, throughout the process: <ul style="list-style-type: none"> • held a large number of meetings⁵ with individuals and groups of preparers, users, actuaries, auditors, regulators and others in order to test proposals and to understand concerns raised by affected parties. • appeared at many public events to exchange views with constituents. • maintained a regular and active dialogue with regulators, standard setters and industry representative groups • obtained the views of users of financial statements through targeted meetings and attendance at user forums in the US, Europe and Asia.

⁵ Over 340 meetings since the ED was published.

<i>Step</i>	<i>Required/Optional</i>	<i>Metrics or evidence</i>	<i>Protocol for and evidence provided to DPOC</i>	<i>Actions</i>
Webcasts and podcasts to provide interested parties with high level updates or other useful information about specific projects	Optional	Number of and participation in webcasts	DPOC receives a report on outreach activities	<p>Staff and board members have recorded 15 podcasts since the end of the exposure draft period and presented four webcasts.</p> <p>The webcasts introduced the exposure draft and discussed the accounting for reinsurance contracts. The podcasts summarise the insurance contracts meetings for each month and places those decisions in context.</p>
Public discussions with representative groups	Optional	Number of discussions held	DPOC receives a report on outreach activities	The staff thinks that the public roundtables and insurance working group meetings, together with discussions with representative groups in private meeting, make it unnecessary to hold public discussions with representative groups.
Online survey to generate evidence in support of or against a particular approach	Optional	Number and results of surveys	DPOC receives a report on outreach activities	The staff thinks that the public roundtables and insurance working group meetings, together with discussions with representative groups in private meeting, make this step unnecessary.
IASB hosts regional discussion forums, where possible, organised with national standard-setters	Optional	Number of meetings held	DPOC receives a report on outreach activities	This step overlaps with the roundtable meetings, which were organised in conjunction with the Accounting Standards Board of Japan, and the US Financial Accounting Standards Board. In addition, staff and board members have presented at regional discussion forums in Europe, South Africa and Canada.

<i>Step</i>	<i>Required/Optional</i>	<i>Metrics or evidence</i>	<i>Protocol for and evidence provided to DPOC</i>	<i>Actions</i>
Round-table meetings between external participants and members of the IASB	Optional	Number of meetings held	DPOC receives a report on outreach activities	In December 2010, after the publication of the ED, the IASB conducted six public roundtables, in Japan, USA and London. These were attended by 94 participants from 81 organizations in 9 countries, representing a wide variety of constituents (including users, preparers, auditors and others). Updates on this project were included in regular reports to the DPOC, and we plan to report a summary of due process at the next trustee meeting.
Drafting quality assurance steps are adequate	Required	Translations team included in review process	DPOC receives summary report on due process steps followed before an IFRS is issued	To be done in due course
Drafting quality assurance steps are adequate	Required	XBRL team included in review process	DPOC receives summary report on due process steps followed before an IFRS is issued	To be done in due course
Drafting quality assurance steps are adequate	Optional	Review draft made available to members of IFASS and comments collected and considered by the IASB	DPOC receives summary report on due process steps followed before an IFRS is issued	To be done in due course
Drafting quality assurance steps are adequate	Optional	Review draft posted on project website	DPOC receives summary report on due process steps followed before an IFRS is issued	The IASB has indicated that a review draft would be made available if it decides that a re-exposure draft is not necessary. This is discussed in agenda paper 16D for the September meeting.
Due process steps reviewed by IASB	Required	Summary of all due process steps discussed by the IASB before an IFRS is issued.	DPOC receives summary report on due process steps before an IFRS is issued.	This paper reviews the due process steps followed

<i>Step</i>	<i>Required/Optional</i>	<i>Metrics or evidence</i>	<i>Protocol for and evidence provided to DPOC</i>	<i>Actions</i>
Exposure draft has appropriate comment period	Required	IASB sets comment period for response Any period outside the normal comment period requires explanation from IASB to DPOC, and subsequent approval	DPOC receives notice of any change in comment period length and approval if required	We plan to ask the IASB for permission to ballot and the appropriate comment period at a future meeting.

Appendix D: Finalisation of an IFRS on insurance contracts, Practice Chapter or Conceptual Framework chapter – Due process steps followed

In agenda paper 16D we discuss whether the proposals in the insurance contracts project can be finalised or whether the IASB should re-expose the revised insurance contract standard. This appendix shows how the IASB has complied with the due process steps that would be required if it were to decide to finalise a standard on insurance contracts. There is substantial overlap between the due process steps that would be required for a revised exposure draft (set out in appendix C) and for a final standard (set out in this appendix). We have highlighted in blue text the rows that are common between this table and Appendix C.

<i>Step</i>	<i>Required/ Optional</i>	<i>Metrics or evidence</i>	<i>Protocol for and evidence provided to DPOC</i>	<i>Actions</i>
Consideration of information gathered during consultation				
IASB posts all comment letters received in relation to the Exposure Draft on the project pages.	Required if request issued	Letters posted on project pages	IASB reports on progress as part of the quarterly report at Trustee meetings, including summary statistics of respondents.	During a 123 days comment period, the IASB received 247 ⁶ comment letters. The letters are available on the public website. A comment letter summary, also available on the public website, was presented to the IASB and FASB in January 2011. Progress to be reported at the next trustee meeting.
Round tables between external participants and members of the IASB.	Optional	Number of meetings held	DPOC receives a report on outreach activities	In December 2010, after the publication of the ED, the IASB conducted six public roundtables, in Japan, USA and London. These were attended by 94 participants from 81 organizations in 9 countries, representing a wide variety of constituents (including users, preparers, auditors and others). Updates on this project were included in regular reports to the DPOC, and we plan to report a summary of due process at the next trustee meeting.

⁶ Some comment letters have been received in parts. As a result of administrative inconsistencies, some were labelled as sub-parts (eg 2, 2A, 2B, 2C) and others had separate numbers (eg 4 and 114). In total the IASB received 253 letters from 247 respondents

<i>Step</i>	<i>Required/ Optional</i>	<i>Metrics or evidence</i>	<i>Protocol for and evidence provided to DPOC</i>	<i>Actions</i>
<p>Board meetings held in public, with papers available for observers. All decisions are made in public session.</p>	<p>Required</p>	<p>Number of meetings held to discuss topic.</p> <p>Project website contains a full description with up-to-date information on the project.</p> <p>Meeting papers posted in a timely fashion.</p> <p>Number of meetings with Consultative Group and confirmation that critical issues have been reviewed with Consultative Group</p>	<p>IASB discusses progress on major projects, in relation to the due process being conducted, with DPOC.</p> <p>IASB review with DPOC its due process over project life cycle, and how any issues regarding due process have been/are being addressed.</p> <p>DPOC meets with the Advisory Council to understand perspectives of stakeholders.</p> <p>DPOC reviews and responds to comments on due process as appropriate.</p>	<p>Board meetings</p> <p>The IASB discussed the project at every meeting between December 2010 and July 2012. The IASB also intends to discuss the project at its September and October 2012 meetings.</p> <p>Project website</p> <p>The project website contains a full description with up-to-date information on the project. In addition to the standard posting of papers, decision summaries and board meeting webcasts, this has included regularly updated material as follows:</p> <ul style="list-style-type: none"> • A high level summary of progress on the project, describing the main IASB decisions • A high level comparison of the IASB’s tentative decisions with the proposals in the ED • A detailed summary of the IASB’s decisions, that shows how each paragraph in the exposure draft would be affected by the decisions taken each month. • A 10-15 minute podcast that summarises the insurance contracts meetings for each month and places those decisions in context. • Topic reports on the IASB’s decisions and working drafts. <p>Meetings with consultative groups</p> <p>See outreach meetings</p> <p>DPOC</p> <p>The Due Process Oversight Committee was informed of progress in the project in March 2011, June 2011, July 2011, October 2011 and April 2012. In addition, in January 2012, the Due Process Oversight Committee was informed about correspondence with the HUB Global Insurance Group regarding the accounting for short-duration insurance contracts.</p>

<i>Step</i>	<i>Required/ Optional</i>	<i>Metrics or evidence</i>	<i>Protocol for and evidence provided to DPOC</i>	<i>Actions</i>
Analysis of likely effects of the forthcoming IFRS or major amendment, for example, costs or on-going associated costs.	Required	Publication of effect analysis	<p>IASB reviews with DPOC results of effect analysis and how it has considered such findings in proposed IFRS.</p> <p>IASB provides a copy of the effect analysis to the DPOC at the point of standard's publication.</p>	<p>Updates on this project were included in regular reports to the DPOC, and we plan to report a summary of due process at the next trustee meeting.</p> <p>The IASB has paid particular attention to the proposals would have on the volatility of reported results. The IASB plans to include an analysis of likely effects in the Basis for Conclusions to a revised exposure draft, or as a standalone document published with a review draft. A preliminary effects analysis is provided in Appendix B of this paper and the IASB plans to provide a copy of the effect analysis to the DPOC in due course.</p>

<i>Step</i>	<i>Required/Optional</i>	<i>Metrics or evidence</i>	<i>Protocol for and evidence provided to DPOC</i>	<i>Actions</i>
Email alerts are issued to registered recipients	Optional	Evidence that alerts have occurred	DPOC receives a report on outreach activities	Interested parties have been notified when updates to the insurance contracts pages are made using subscriber email alerts. At last count there were over 13,000 subscribers to the insurance contracts email alert.
Outreach meetings to promote debate and hear views on proposals published for public comment	Optional	Number of meetings, including efforts aimed at investors	DPOC receives a report on outreach activities.	<p>IASB members and staff have, throughout the process:</p> <ul style="list-style-type: none"> held a large number of meetings⁷ with individuals and groups of preparers, users, actuaries, auditors, regulators and others in order to test proposals and to understand concerns raised by affected parties. appeared at many public events to exchange views with constituents. maintained a regular and active dialogue with regulators, standard setters and industry representative groups obtained the views of users of financial statements through targeted meetings and attendance at user forums in the US, Europe and Asia. <p>Meetings with consultative groups</p> <p>Since the end of the comment period, the IASB consulted in public with the Insurance Working Group in November 2010, March 2011, May 2011, October 2011 and June 2012 meeting for a total of 6.5 days. The working group papers covered the all aspects of the proposed IFRS including scope, unbundling, recognition, contract boundary, cash flows, discount rate, risk adjustment, residual margin, participating contracts, reinsurance assets, premium allocation approach, disaggregation and volume information, OCI, disclosures and transition.</p>
IASB organise regional discussion forums organised with national standard-setters	Optional	Number of meetings held	DPOC receives a report on outreach activities	This step overlaps with the roundtable meetings, which were organised in conjunction with the Accounting Standards Board of Japan, and the US Financial Accounting Standards Board. In addition, staff and board members have presented at regional discussion forums in Europe, South Africa and Canada.

⁷ Over 340 meetings since the ED was published.

<i>Step</i>	<i>Required/ Optional</i>	<i>Metrics or evidence</i>	<i>Protocol for and evidence provided to DPOC</i>	<i>Actions</i>
Finalisation				
Need for re-exposure of standard considered	Required	An analysis of the need to re-expose is considered at a public IASB meeting, using the agreed criteria	IASB discusses its thinking on the issue of re-exposure with the DPOC	Agenda paper 16D for the September meeting discusses the need for re-exposure.
IASB sets an effective date for standard, considering the need for effective implementation, generally providing at least a year.	Required	Effective date set, with full consideration of implementation challenges	The IASB discusses any proposed shortening of the period for effective application with the DPOC	A paper considering the effective date of the proposed amendments will be presented at the October 2012 IASB meeting.
Drafting quality assurance steps are adequate	Required	Translations team included in review process	DPOC receives summary report on due process steps followed before an IFRS is issued	To be done in due course
Drafting quality assurance steps are adequate	Required	XBRL team included in review process	DPOC receives summary report on due process steps followed before an IFRS is issued	To be done in due course
Drafting quality assurance steps are adequate	Optional	Review draft made available to members of IFASS and comments collected and considered by the IASB	DPOC receives summary report on due process steps followed before an IFRS is issued	To be done in due course

<i>Step</i>	<i>Required/ Optional</i>	<i>Metrics or evidence</i>	<i>Protocol for and evidence provided to DPOC</i>	<i>Actions</i>
Drafting quality assurance steps are adequate	Optional	Review draft posted on project website	DPOC receives summary report on due process steps followed before an IFRS is issued	IASB has indicated that a review draft would be made available if it decides that a re-exposure draft is not necessary. This is discussed in agenda paper 16D for the September meeting.
Due process steps reviewed by IASB	Required	Summary of all due process steps discussed by the IASB before an IFRS is issued.	DPOC receives summary report on due process steps before an IFRS is issued.	This paper reviews the due process steps followed