AICPA

Working Draft

Targeted Improvements to Long-Duration Contracts Implementation Paper

Issue #16: **Level of Aggregation for the Measurement of the Liability for Future Policy Benefits.**

Wording to be Included in the Audit and Accounting Guide: Life and Health Insurance Entities.

Initial Measurement – Long-Duration Contracts

1. FASB ASC 944-40-30-7 states,

> The liability for future policy benefits accrued under paragraph 944-40-25-8 shall be the present value of future benefits to be paid to or on behalf of policyholders and related expenses less the present value of future net premiums (portion of gross premium required to provide for all benefits and expenses, excluding acquisition costs or costs that are required to be charged to expense as incurred). That liability shall be estimated using methods that include assumptions, such as discount rate, mortality, morbidity, terminations, and expenses (see paragraphs 944-40-30-9 and 944-40-30-11 through 30-15). The liability also shall consider other assumptions relating to guaranteed contract benefits, such as coupons, annual endowments, and conversion privileges. The assumptions shall not include a provision for the risk of adverse deviation. In determining the level of aggregation at which reserves are calculated, an insurance entity shall not group contracts together from different issue years but shall group contracts into quarterly or annual groups.

2. FASB ASC 944-40-30-7 requires the determination of the level of aggregation for measurement of the liability for future policy benefits (referred to herein as the “cohort”) on initial measurement. FASB ASC 944-40-35 on subsequent measurement does not address changes in established cohorts. FinREC believes that the determination of a cohort is not an accounting principle or a method of applying an accounting principle. Further, FinREC believes that a cohort is not an estimate that is evaluated for updates and changed based on new information, as needed (i.e. a cohort is not a cash flow or discount rate assumption where updates are required at least annually), as described in ASC 944-40-35-6A. Therefore, FinREC believes that a cohort is a decision made at initial measurement and cannot be changed once established.

3. Consistent with the guidance in FASB ASC 944-40-30-7, FinREC believes that for a cohort, an issue year is any period of twelve consecutive months and is not required to be consistent with either a calendar year or the insurance entity’s annual reporting period. FinREC also believes that the objective of the requirement in ASC 944-40-30-7 to "not group contracts together from different issue years" is to limit the aggregation of contracts within a cohort to contracts written within a maximum period of twelve months. This is consistent with the comment in BC48 of ASU 2018-12 that “grouping on an annual basis is a minimum requirement” for the measurement of the liability for future policy benefits. Therefore, FinREC believes it is acceptable for an insurance entity to

aggregate contracts written within any period less than twelve months for the measurement of the liability for future policy benefits.

4. In addition to the limit by issue year, FinREC believes that contracts accounted for under different accounting models within the guidance in FASB ASC 944 (e.g., traditional vs. limited-payment long-duration contracts) or those that have cash flows with different currencies (e.g., USD, Euro, Yen), should not be aggregated in the same cohort for measuring the liability for future policy benefits.

5. FinREC believes that it may be useful for an insurance entity to consider the type of risk covered (e.g., mortality, morbidity or other insurance risk) and duration of coverage (e.g., 10 year vs. 30 year term) in determining the cohort for measuring the liability for future policy benefits.

6. In determining the cohort as required in FASB ASC 944-40-30-7, in addition to the limit by issue year, and the factors noted in paragraphs 4 and 5, FinREC believes that the disclosure aggregation guidance in FASB ASC 944-40-50-5A, and in FASB ASC 944-40-55-13F through 55-13H may be useful in determining groupings for measurement purposes. FASB ASC 944-40-50-5A notes that an insurance entity "shall aggregate or disaggregate the disclosures required by FASB ASC 944-40-50-6 through 50-7C so that useful information is not obscured by … the aggregation of items that have significantly different characteristics." In addition, FASB ASC 944-40-55-13F through 55-13H provide examples of categories to consider for disclosure aggregation including types of coverage, geography, and market or type of customer.

7. Subsequent changes in reportable segments do not override the guidance in paragraph 2 that does not permit changes in the level of aggregation for which reserves are calculated for established cohorts.

8. FinREC believes the concepts regarding characteristics of the contracts for aggregation purposes as discussed in paragraphs 3 - 6 should be considered each reporting period for new contracts that are written. While consistency in applying this guidance would often result in a consistent level of aggregation across different policy issue years, FinREC believes that the current policy issue year is not required to be aggregated in a similar manner to prior policy issue years.

Transition

9. FASB ASC 944-40-65-2(d)(6) states

> For contracts in force issued before the transition date, an insurance entity shall not group contracts together from different original contract issue years but shall group contracts into quarterly or annual groups on the basis of original contract issue date for purposes of calculating the liability for future policy benefits. For acquired contracts, the acquisition date shall be considered the original contract issue date.

10. When establishing cohorts for contracts issued before the transition date under FASB ASC 944-40-65-2(d)(6), FinREC believes that insurance entities should consider the same concepts regarding characteristics of the contracts for aggregation purposes as discussed in paragraphs 2 – 6.

Comments should be received by July 29, 2021, and sent by electronic mail to Kim Kushmerick at kim.kushmerick@aicpa-cima.com, or you can send them by mail to attention: Kim Kushmerick, 1345 Avenue of the Americas, New York, N.Y., 10105.