



April 3, 2002

Letter of Comment No: 25
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Date Received: 4/4/02

Mr. Timothy S. Lucas
Director of Research and Technical Activities
Financial Accounting Standards Board
401 Merrit 7, P.O. Box 5116
Norwalk, CT 06856-5116

Re: Proposal for a New Agenda Project
Issues related to the Recognition of Revenues and Liabilities (Proposed Project)

Dear Mr. Lucas:

The GAAP Financial Reporting Principles Subcommittee (the Committee) of the American Council of Life Insurers (ACLI) appreciates the opportunity to provide its comments to the Financial Accounting Standards Board concerning the Proposed Project. The ACLI is the principal trade association of life insurance companies, representing 399 members that account for, in the aggregate, 75 percent of the assets of legal reserve life insurance companies in the United States.

In general, the Committee is supportive of the FASB's efforts to provide timely guidance about revenue and liability recognition issues. In particular, the Committee would welcome additional guidance with respect to liability recognition, but does not believe that additional guidance is needed with respect to liabilities arising out of insurance contracts as discussed below. The Committee is concerned about the potential implications to the long-standing interrelated accounting methodologies already established in existing insurance industry accounting standards. In that regard, the Committee believes that the guidance in FASB Statements No. 60, *Accounting and Reporting by Insurance Enterprises*, No. 97, *Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sales of Investments*, No. 113, *Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts*, and No. 120, *Accounting and Reporting by Mutual Life Insurance Enterprises and by Insurance Enterprises for Certain Long-Duration Participating Contracts*, is still appropriate. Those standards represent interrelated models of revenue, expense, asset and liability recognition and valuation that have been developed over many years and, in the

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aggregate, comprise the comprehensive accounting and reporting model for insurance enterprises.

Under the established guidance, insurance contracts are classified within standard classes of contracts that dictate the appropriate method for revenue recognition and liability measurement.

For example:

- Statement No. 60 is applicable to certain insurance contracts¹ issued by stock life insurance enterprises and property and liability insurance enterprises with limited applicability to mortgage guaranty insurance enterprises. Insurance contracts are classified as short-duration or long-duration, and accounting and reporting standards are provided for each contract classification. The standards include specific guidance for premium recognition and liability measurement by classification type.
- Statement No. 97 provides accounting and reporting standards for three classes of long-duration insurance contracts (investment contracts, limited-payment contracts, and universal life-type contracts), including revenue recognition and liability measurement.
- Statement No. 113 provides guidance for accounting by insurance enterprises for the reinsuring of insurance contracts, including revenue recognition, gain/loss recognition and the reporting of liabilities related to reinsurance transactions.
- Statement No. 120 extends the guidance in the above listed statements to mutual life insurance enterprises which, accordingly, includes revenue recognition and liability measurement.
- AICPA Statement of Position 98-7, *Deposit Accounting*, provides guidance about how to account for insurance and reinsurance contracts that do not transfer insurance risk, including revenue recognition.

In addition, specific guidance for new and complex insurance products developed and sold by insurance entities subsequent to the issuance of Statement No. 97 is in the final stages of development by an AICPA task force. The proposed draft Statement of Position (proposed draft SOP) is entitled: *Accounting and Reporting by Insurance Enterprises for Certain Nontraditional Long-Duration Contracts and for Separate Accounts*, and has its conclusions based upon the existing "level A" FASB guidance.

We believe that including insurance in the Proposed Project has the potential to complicate and confuse the accounting for insurance contracts, especially if any changes are made in the recognition and measurement of insurance-related revenues and liabilities. Any changes to the current accounting model would not serve to increase the understanding of insurance enterprises' earnings results. Accordingly, the Committee believes that an appropriate insurance industry accounting model already exists for the recognition and measurement of revenues and liabilities

¹ Insurance contracts as referred to in this letter include the following: short- and long-duration life, A&H, disability, long-term care and other health insurance contracts which include mortality and morbidity risk and property and liability insurance contracts; as well as investment contracts, limited-payment contracts and universal-life type contracts.

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arising out of insurance contracts, and that insurance contracts should be excluded from the scope of this Proposed Project. Further, the Committee continues to support an accounting model that focuses on "earnings". We believe that the *earned* criterion contained in the current insurance-related accounting model as well as the additional guidance included in the proposed draft SOP is the best approach for the insurance industry since the insurance enterprise is required to have "substantially accomplished" its contractual obligations, or have been released from risk, to be entitled to recognize a benefit in earnings. For this reason the Committee opposes any accounting model that has the potential to "front end" the recognition of revenue at the time of the product sale. We do not believe that such a model is appropriate, especially in today's environment where there is a lack of trust in reported earnings. Consequently, we strongly encourage the Board to move cautiously and deliberately with respect to this Proposed Project, avoiding the recognition of revenues before contractual obligations have been performed and remaining faithful to the concept that earnings occur as such obligations are performed.

We thank you for the opportunity to comment on the Proposal and would be pleased to discuss our comments with the Board or its staff at its convenience.

Sincerely,

Paul S. Graham, III
Chief Actuary
American Council of Life Insurers