Baldwin & Lyons, Inc.

Michael B. Edwards
Assistant Vice President

1099 North Meridian Street
Indianapolis, IN 46204
(317) 636-9800

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Financial Accounting Standards Board
Technical Director
401 Merritt 7
Norwalk, CT 06856-5116

RE: File Reference No. 2013-290, Insurance Contracts (Topic 834)

Dear Members of the Financial Accounting Standards Board:

Thank you for the invitation to comment on the FASB Insurance Contracts (Topic 834) Exposure Draft ("FASB ED"). Baldwin & Lyons, Inc., is a small (market cap $375 million) specialty property-casualty insurer involved in providing liability coverage for large and medium-sized trucking and public transportation fleets as well as coverages for trucking industry independent contractors and several other products. Our comments will relate specifically to the FASB ED's impact on the P&C industry.

We believe that the FASB ED, as proposed, would fundamentally and materially alter historical financial accounting reporting for insurers without concern for the historical users of the financials. We believe that current U.S. GAAP insurance accounting comprehensively addresses accounting for insurance contracts. Additionally we believe that U.S. GAAP insurance accounting is "not broken", is the international standard and should be maintained. As such, we propose that the FASB reject the FASB ED as currently proposed. This letter will articulate our reasoning and rationale for rejection of the FASB ED.

Estimating Cash Flows and Discounting

We believe that the P&C industry is not served in any positive way by moving toward current-value accounting through the use of discounted estimated future cash flows to approximate present value. Our consensus is that the introduction of discounting does not produce useful decision making information but, to the contrary, diminishes the understanding and obfuscates the measurement of periodic claim reserve changes. The current, long-standing measurements of loss reserve development are clearly understood and heavily relied upon by all users of the financial statements of P&C companies. We believe that the new measures would render all historical data bases useless and would require companies to continue to publish data in the current format even though it would no longer be considered to be GAAP compliant.

Discounting also adds additional unwarranted subjectivity to the estimation of the claim reserves. Discounting will change the reporting framework with changes in interest rates and assumptions regarding cash flows driving earnings and equity as opposed to underwriting earnings driving equity.

Claim reserves are typically held rather than traded or liquidated early. There is no true market for the routine early extinguishment of insurance contracts. Accordingly, discounting claim reserves is an abstract and uncertain concept and is not useful in determining the value of this liability. Even gradual quarterly changes in the discount rate or the estimate of cash flows could create material earnings and/or equity volatility with no underlying changes in the liability itself.

We believe the current P&C accounting for short-duration contracts for ultimate claim estimates, developed and refined using a variety of deterministic projection methods, is time-tested and historically validated using actuarially accepted projections. In contrast, the FASB ED proposed replacement with one stochastic model has not been vetted nor validated. P&C reserving has been and should be focused on estimating the ultimate best estimate of losses and on reserve adequacy as opposed to using a single model with estimations of the timing of claim payments. For many years, the P&C industry has projected ultimate settlement estimates using multiple actuarially sound projection methods and then judgmentally reviews the methods based on the actuaries' judgment about the strength of each projection after reviewing the facts and circumstances. The proposed model inserts undue difficulty and complexity to the estimating of the loss and loss adjustment expenses by requiring the estimation of the timing of cash flows from all aspects of the fulfillment process to include the following: claim payments, ceded recoveries, assumed reinsurance, reinstatement premiums, salvage and subrogation and litigation. Most P&C companies have not tracked the timing of the inputs necessary for the proposed model nor is the historical cash flow information even available within many insurance companies, ours included. Further, the fact that our company writes high limit commercial automobile business which attaches excess of significant self-insured retentions, results in highly volatile cash flows which are not conducive to reliable prediction, even if historical data was available. Accordingly, we believe that estimated payment patterns would largely not be reliable for many commercial liability products. Instead, measuring and relying on projected cash flows rather than estimating ultimate reserves adds increased bias, variation and judgment with no offsetting benefits. In reality, the precision of the reserving is reduced to an academic model and the accuracy of the estimated ultimate reserves is reduced and the variability has been increased.

Insurance companies will be negatively impacted in the process of supporting the revised accounting by the creation of new system purchases, major revisions of old systems, creation of new reports, spreadsheets and procedures to provide support for the fulfillment cash flows and discounting. Additionally, management will be required to continuously update and revise the expected cash flow and loss payment patterns quarterly, and maintain historical periods. Tracking and updating the new variables will exponentially increase the financial accounting costs compared to the current accounting method. In short, there will be a significant addition to expense to provide users of the financial statements with a far less understandable product.

Investors

We believe that the investing community is not served well by moving to an accounting system focused on the discounted liquidation accounting which deprives outside investors of established U.S. GAAP results which have provided relevant, tested and calibrated historical financial information to assist in the review of the financial results and of the ultimate assessment of insurers as going concern. P&C investors value insurance companies based of the company's book value and the return on equity. The impact of current value accounting would become a major driver of adjustments to earnings volatility and book value, thus potentially disrupting the trading of these securities.

Investors also evaluate the adequacy of the recorded ultimate claim reserves as opposed to the academic calculation of the present value of the claim reserves. Therefore the investment community would be negatively impacted by moving toward a focus on the liquidation value (real or theoretical). The investment community is better served with undiscounted financial results that are understandable and are not arbitrarily impacted by discounting. Additionally, the discounting impacts the comparability in reserves and reserve development between the balance sheet, footnotes and the statutory schedule P. As a result, the FASB ED hinders the investment community from adequately comparing and assessing the adequacy of balance sheet claim reserves as the claim reserves footnote and the statutory schedule P would be calculated on inconsistent measurement bases.

Ultimately, the investing community is negatively impacted when discounting forces preparers to produce financial statements for the objective to comply with the new standard as opposed to serving the interests of the general purpose financial statement users. Further, the FASB ED will also introduce the opportunity for manipulation of financials statements through changes in assumptions, which will put a meaningfully larger burden on independent auditors, again increasing compliance expenses without benefit.

Consistency and Comparability

We believe that the P&C industry is not served well by moving away from current U.S. GAAP insurance accounting which is currently aligned with the business models of P&C insurers and is how P&C insurers, in fact, manage their business and evaluate financial operating performance. P&C insurers, regulators and investors evaluate profitability of insurers through the review of the underwriting results (premiums less claim costs and expenses). We believe that the U.S. GAAP insurance accounting is superior to the FASB ED and the current U.S. GAAP insurance accounting provides historically proven and time-tested actuarial results as opposed to the FASB ED which is decidedly theoretical and unproven. The FASB ED will introduce increased artificial volatility in insurers' earnings and equity without an equivalent benefit. This will lead to diminished comparability between P&C insurance companies. Historical key performance indicators, including earnings per share, combined ratio and other industry and company data, would be irreconcilable with all future results.

Conclusion

We believe that the P&C industry is well served with current U.S. GAAP. We believe that existing guidance is reasonable and appropriate and there is no practical evidence of the need for a complete revision of accounting for insurance contracts. Rather we are a proponent of measured improvements to accounting for insurance contracts only after compelling evidence supporting such revisions is accepted by issuers, analysts, investors and other users of the financial statements. As such, we propose that the FASB reject the FASB ED, as currently proposed, in its entirety.

Thank you for considering our comments.

Sincerely,

Michael Edwards

Michael B. Edwards
Assistant Vice President
Baldwin & Lyons, Inc.