



AMERICAN ACADEMY *of* ACTUARIES

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Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, Connecticut 06856-5116
Via email: director@fasb.org

The Life Financial Reporting Committee and Financial Reporting Committee of the American Academy of Actuaries¹ are pleased to provide comments to the Financial Accounting Standards Board (FASB) concerning Exposure Draft *Proposed ASU—Financial Services—Insurance (Topic 944): Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts*.

A major aspect of the actuarial profession's expertise is the valuation of deferred policy acquisition cost assets related to insurance contracts. We agree with the general conclusion that costs that are (1) incremental direct costs of contract acquisition and (2) directly related to specific activities performed by the insurer for the contract should be capitalized. We also believe that the actuarial aspects of the proposed guidance will be operational and not unduly costly. However, we do have concerns regarding some of the specifics of the proposed guidance, such as the disparate treatment of non-incremental, direct costs depending on whether the costs represent salary or employee benefits versus other types of costs.

Our specific comments to each of the questions posed by the Exposure Draft follow. Thank you again for this opportunity to provide input.

Sincerely,

Leonard J. Reback, MAAA, FSA
Chairperson, Life Financial Reporting Committee
American Academy of Actuaries

Rowen B. Bell, MAAA, FSA
Chairperson, Financial Reporting Committee
American Academy of Actuaries

¹ The American Academy of Actuaries ("Academy") is a 16,000-member professional association whose mission is to serve the public on behalf of the U.S. actuarial profession. The Academy assists public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.

1. We agree with the conclusion that costs that are (1) incremental direct costs of contract acquisition and (2) directly related to specific activities performed by the insurer for the contract should be capitalized. However, we do not understand why the capitalized costs that are directly related to specific activities performed by the insurer for the contract should be limited to compensation and payroll-related fringe benefits. As discussed further in our response to question 2, we believe that costs incurred for equipment, occupancy and supplies used by these employees should also be eligible for capitalization, as should travel, and meal and entertainment expenses incurred by them in the course of securing a sale. This should be subject to the requirement that the costs be incurred during the time spent performing acquisition activities for a contract that has actually been acquired or otherwise meet the criteria discussed further in our response to question 2.

Capitalizing costs as described above would provide an appropriate deferred acquisition cost asset. In addition, the resulting Topic 944 liability net of such a deferred acquisition cost asset would appropriately reflect the net obligation under the contract. Furthermore, it is important that there be consistency between the treatment of acquisition costs for insurance contracts and the treatment of transaction costs for financial instruments, such as loan receivables under Topic 310. An inconsistency between the treatment of insurance contract transaction costs and financial instrument transaction costs would place undue stress on the dividing line between the definition of an insurance contract and the definition of a financial instrument. Expensing certain such costs for insurance contracts would also inappropriately penalize such contracts relative to financial instruments.

We believe that these considerations also apply to the separate joint IASB/FASB insurance contracts project. In that project, the residual or composite margin under the proposed insurance contracts model would then be calibrated to the premium net of the acquisition costs described here.

We believe that the proposed guidance is operational.

2. With the exception of the distinction between payroll-related costs and non-payroll related costs, we believe that the criteria set forth in AcSEC Statement of Position 93-7, *Reporting on Advertising Costs (93-7)*, for capitalizing direct response advertising costs represent an appropriate basis for capitalizing insurance contract transaction costs or acquisition costs in general. Among widely used insurance contract distribution channels, the direct response channel is the most susceptible to costs related to unsuccessful efforts. With the exception of the distinction between payroll-related costs and non-payroll related costs, both of which we believe should be eligible for capitalization, we do not believe that direct response acquisition or transaction costs should be treated differently from similar costs incurred when selling other types of product through direct response distribution. And other than that exception, we would be concerned that certain distribution channels may be unduly disfavored if different capitalization rules apply to different distribution channels.

The distinction between payroll-related and non-payroll related costs is not appropriate for most forms of insurance contract distribution, although it does not materially impact direct response distribution. In other forms of insurance contract distribution, variable expenses that would not necessarily meet the definition of an “incremental cost” are incurred by employees in the course of acquiring contracts for items such as travel, entertainment, supplies and equipment, which is generally not the case for direct response distribution. Therefore, the distinction between payroll-related and non-payroll related expenses enumerated in SOP 93-7 is not appropriate for insurance contract acquisition costs in general.

3. We agree that advertising costs, with the exception of direct response solicitation costs covered by paragraph 41 of SOP 93-7, should not be capitalized. Advertising costs only indirectly impact sales, and thus are of the nature of overhead costs.
4. We do not express an opinion about the costs to comply with these amendments, since most of the cost will likely be incurred through updating accounting information systems, rather than actuarial systems. Regardless of the cost, however, we are not sure of the value of imposing these costs so close to the anticipated complete overhaul of the insurance accounting model.
5. We are not aware of any issues that would make these amendments non-operational from the standpoint of updating actuarial systems. However, most of the information required to comply with the proposed amendments would need to be obtained from accounting information systems, and we do not express an opinion about the operability of those required changes. But even if these changes are operational, with an effective date so close to an anticipated complete overhaul of the insurance accounting model, it is unclear if these changes would be worthwhile.