Institute of Chartered Accountants of New Zealand

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LIFE INSURANCE BUSINESS

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This Financial Reporting Standard should be read in the context of the Explanatory Foreword to General Purpose Financial Reporting published by the Council, Institute of Chartered Accountants of New Zealand.

The Accounting Standards Review Board has approved FRS-34: Life Insurance Business, for the purposes of the Financial Reporting Act 1993, to apply to the general purpose financial reports of all life insurers (as defined in the Standard).

The definitions are in Section 21. Financial reporting standards are paragraphs in bold type-face in this Standard. Where appropriate, interpretive commentary paragraphs in plain type-face follow the financial reporting standards.

The paragraph numbering in this standard is the same as the numbering of AASB-1038: Life Insurance Business. Where there is an Australian requirement but no corresponding New Zealand requirement a paragraph number will be given, followed by the words "Not Used".

MAIN FEATURES OF THE STANDARD

The Standard:

(a) applies to life insurers and to the parent entity of groups that include a life insurer

(b) requires a life insurer and the parent entity of a life insurer to include in its financial statements all its assets, liabilities, revenues, expenses and equity irrespective of whether they are designated as relating to policyholders or to shareholders

(c) requires all assets of a life insurer to be measured at net market values

(d) requires all liabilities of a life insurer to be measured at net present values, and describes the key parameters for measuring policy liabilities

(e) requires a life insurer that is a parent entity of a group to recognise and disclose any excess (which will include any internally generated goodwill) or deficiency of the net market values of interests in subsidiaries over the net assets of those subsidiaries recognised in the consolidated financial statements, in the financial statements of the life insurer group

(f) requires premiums and claims to be separated on a product basis into their revenue, expense and change in liability components unless the separation is not practicable or the components cannot be reliably measured, subject to a transitional provision

(g) requires returns on all investments controlled by a life insurer to be recognised as revenues

(h) requires participating benefits vested in relation to the reporting period, other than transfers from unvested policyholder benefits liabilities, to be recognised as expenses

(i) requires reinsurance contracts to be recognised on a gross basis

(j) requires specific disclosures in the financial reports prepared by life insurers or groups which include a life insurer.

1 APPLICATION

STANDARD

1.1 This Standard applies to the general purpose financial reports of:

(a) each life insurer; and

(b) each group which includes a life insurer.

COMMENTARY

1.1.1 This Standard applies to the consolidated financial statements of a group in relation to a life insurer subsidiary. Paragraph 5.2 is of particular relevance in these cases. This Standard does not apply to reporting by a group for its activities other than its life insurance business. In measuring and reporting business other than life insurance business as well as aspects of life insurance business where this Standard contains no requirements, a group that includes a life insurer should follow appropriate financial reporting standards.

STANDARD

1.2 In the event of a conflict between this Standard and any other Standard, the requirements of this Standard prevail.

1.2.1 "*Not Used*"

COMMENTARY

1.2.2 This Standard requires all assets of life insurers to be measured at net market value. This requirement means that life insurers do not apply Standards that are predicated on the historical cost or modified historical cost bases of accounting. For this reason, for example, the use of net market values in measuring assets means that life insurers do not depreciate assets in accordance with SSAP-3: *Accounting for Depreciation*, revalue assets in accordance with SSAP-28: *Accounting for Fixed Assets*, recognise and amortise goodwill or use the equity method of accounting in accordance with SSAP-8: *Accounting for Business Combinations*, and recognise leases in accordance with SSAP-18: *Accounting for Leases and Hire Purchase Contracts*.

1.2.3 FRS-21: *Accounting for the Effects of Changes in Foreign Currency Exchange Rates* applies in relation to the translation of transactions, other than foreign currency hedge contracts, and foreign operations. Premiums received and claims paid in foreign currencies would need to be translated according to FRS-21. However, some of the requirements of FRS-21 are not applicable where a net market value basis is used for measuring assets. The effect of movements in exchange rates on the carrying amounts of investments is included in their net market values, changes in which are recognised as part of investment revenue in the statement of financial performance as they occur. Because this applies in the case of foreign branch offices and where the investment is a foreign subsidiary,

there is no recognition of a foreign currency translation reserve. The only case in which a foreign currency translation reserve would be recognised by a life insurer is in the context of its consolidated financial statements where the reserve already exists in the financial statements of a subsidiary which is not a life insurer.

2 OPERATIVE DATE

STANDARD

2.1 This Standard applies to periods ending on or after 31 December 1999.

2.2 "*Not Used*"

2.2.1 "*Not Used*"

3 PURPOSE OF STANDARD

STANDARD

3.1 The purpose of this Standard is to:

(a) prescribe the methods to be used for reporting on life insurance business in the financial report

(b) require disclosures about life insurance business in the financial report.

4 APPLICATION OF MATERIALITY

STANDARD

4.1 The financial reporting standards set out in this standard shall apply to all financial reports where such application is of material consequence. A statement, fact, or item is material if it is of such a nature or amount that its disclosure, or the method of treating it, given full consideration of the circumstances applying at the time the financial report is completed is likely to influence the users of the financial report in making decisions or assessments.

COMMENTARY

4.1.1 An example of the application of materiality is that disclosures about life insurance business in the context of a group that includes a life insurer are required where the life insurance business is material in the context of the group.

4.1.2 For the purposes of FRS-24: *Interim Financial Statements* the determination of policy liabilities in accordance with Section 9 of this Standard does not necessarily require a full actuarial valuation. The policy liability is to be determined on a reliable basis, including a full review of assumptions, and not be materially different from policy liabilities determined by a full actuarial valuation.

5 ENTITY AND CONSOLIDATION ISSUES

The Life Insurer Entity

STANDARD

5.1 A life insurer must recognise in its financial statements the assets, liabilities, revenues, expenses and equity of the entity, whether they are designated as relating to policyholders or to shareholders.

COMMENTARY

5.1.1 Life insurers may have both policyholders and shareholders with a financial interest in the entity. It is sometimes argued that the interests of policyholders and the interests of shareholders form the bases of separate entities that should prepare separate primary financial statements. However, the view adopted in this Standard is that the interests of policyholders and shareholders are intertwined and form the basis of a single entity. The boundaries of this entity are defined by control. The directors of the life insurer, in pursuing its objectives, dominate the decision-making in relation to the financial and operating policies of the life insurer, which includes the assets of the entity, whether they are designated as relating to policyholders or to shareholders.

5.1.2 Equity in a shareholder-owned life insurer will generally comprise only shareholder equity. Although participants in the industry commonly refer to "policyholder retained profits", such amounts are unvested policyholder benefits liabilities. A life insurer will only have policyholder equity if that life insurer has foreign life insurance operations in a jurisdiction that permits retained profits to remain unallocated between policyholders and shareholders, and the policyholders' component cannot be determined.

Financial Reports of Groups that Include a Life Insurer Subsidiary

STANDARD

5.2 The consolidated financial statements of a group that includes a life insurer subsidiary must recognise all of the assets, liabilities, revenues and expenses of that subsidiary, whether they are designated as relating to policyholders or to shareholders of that life insurer. The assets, liabilities, revenues and expenses of a life insurer subsidiary and its group recognised in the consolidated financial statements of a group must be measured in accordance with this Standard.

COMMENTARY

5.2.1 For the same reasons that a life insurer entity is considered to comprise both policyholder and shareholder interests, the view adopted in this Standard is that the parent entity controls the interests of both policyholders and shareholders and, accordingly, the consolidated financial statements of the group includes all of those

interests. The parent entity of a life insurer effectively uses all of the resources of shareholders and policyholders in achieving its objectives and effectively controls policyholder interests for the benefit of both policyholders and shareholders.

5.2.2 Some life insurers are subsidiaries of entities other than life insurers, such as banks, and some are subsidiaries of other life insurers. The character of the parent entity of a life insurer has no bearing on whether consolidated financial statements, prepared in accordance with paragraph 5.2, are required.

Consolidated Financial Statements of Life Insurers and Investments in Subsidiaries and Other Entities

STANDARD

5.3 Any excess of the net market values of interests in subsidiaries (or in-substance subsidiaries and partnerships) over the net amount of subsidiaries' (and other entities') assets and liabilities recognised in the consolidated financial statements must be recognised in the consolidated financial statements of a life insurer as a separate asset.

COMMENTARY

5.3.1 These requirements reflect the life insurance industry's focus on the net market values of investments. In accordance with section 12 of this Standard, assets are to be recognised in a life insurer's financial statements at net market values. Some of these assets may be interests in subsidiaries (or in-substance subsidiaries and partnerships). In a life insurer's consolidated financial statements, the assets and liabilities relating to these interests may be recognised using the amounts in the records of the subsidiaries (and other entities). The net market values recognised in the life insurer's "parent entity" financial statements may exceed the net amounts of the subsidiary's (and other entities') assets and liabilities. The "excess" may comprise the following components:

(a) acquired goodwill, to the extent that it remains at reporting date

(b) increments in the value of goodwill associated with the subsidiaries (or other entities) since the acquisition or establishment of the subsidiaries (or other entities)

(c) measurement differences, resulting from the assets and liabilities included in the life insurer group financial statements being carried in the records of subsidiaries (or other entities) on measurement bases other than those required in this Standard.

Acquired Goodwill

COMMENTARY

5.3.2 Under SSAP-8: *Accounting for Business Combinations*, acquired goodwill, if any, is recognised on preparing consolidated financial statements and is amortised in those statements. However, as indicated in paragraph 5.3.1(a), the separate asset

required to be disclosed by paragraph 5.3 already includes any remaining acquired goodwill. Therefore, this Standard does not require either the separate recognition of acquired goodwill or its amortisation because it would not be relevant to separately recognise it once more on consolidation.

Internally Generated Goodwill

COMMENTARY

5.3.3 The component noted in paragraph 5.3.1(b) is internally generated goodwill. This Standard overrides the generally accepted prohibition on recognising internally generated goodwill. The main reason for prohibiting the recognition of internally generated goodwill is the difficulty, or impossibility, of identifying the events or transactions which contribute to the overall goodwill of an entity. In addition, even if these were identifiable, the extent to which they generate future benefits and the value of such benefits are not usually capable of reliable measurement.

5.3.4 Life insurers take an overall view of their subsidiaries (and other entities) as investments and may not attempt to assign particular values to underlying individual assets and liabilities. A reliable measure of net market value is used to determine the carrying amounts of whole businesses that are investments, with the increments and decrements in carrying amounts recognised as revenues and expenses as they occur. The effective recognition of internally generated goodwill relating to a subsidiary (and other entities) of a life insurer in the life insurer's financial statements is simply one of the facets of a net market value model.

5.3.5 In relation to the life insurance business conducted by the life insurer itself, internally generated goodwill is not recognised. This could only be possible where the interests of policyholders and the interests of shareholders form the basis of separate entities that prepare separate primary financial statements. As noted in paragraph 5.1.1, the view adopted in this Standard is that the interests of policyholders and shareholders are intertwined and form the basis of a single entity. Life insurers use the requirements of this Standard to report on their own life insurance business and would not, for example, use embedded value or appraisal value methods in relation to their own business. A parent entity which is not a life insurer may revalue its investment in a life insurer in the parent entity financial statements in accordance with generally accepted accounting practice.

Deficiency of Net Market Values of Interests in Subsidiaries

STANDARD

5.4 Any change in the deficiency of the net market values of a life insurer's interest in subsidiaries (or in-substance subsidiaries and partnerships) over the net amount of subsidiaries' (and other entities') assets and liabilities included in the consolidated financial statements must be recognised in the

consolidated financial statements of a life insurer as a revenue or an expense only after:

(a) the carrying values of all assets and liabilities of the subsidiary have been reviewed, and remeasured where appropriate; and

(b) any asset recognised in accordance with paragraph 5.3 against which the deficiency must be offset has been eliminated.

COMMENTARY

5.4.1 A deficiency of the net market value of a life insurer's interest in a subsidiary (or in-substance subsidiary or partnership) over the recognised net assets of that subsidiary (or other entity) may conceivably arise, although such a deficiency is expected to be extremely rare. Where such a rare circumstance arises, a life insurer parent entity should review the measurement of the net assets of the subsidiary (or other entity) to ensure that they are recognised and measured in accordance with the requirements of applicable Standards. If the subsidiary's (or other entity's) net assets are over-valued, they should be remeasured. If the deficiency persists after a thorough and complete review, it is offset against any assets arising in respect of other subsidiaries (or other entities) as a result of applying the provisions of paragraph 5.3. The change in any remaining deficiency is recognised as a revenue or an expense in the financial statements of the life insurer group. The remaining deficiency is not recognised as a liability because it does not embody a present obligation.

6 PREMIUMS AND CLAIMS

STANDARD

6.1 Subject to paragraph 6.2, components of premiums that are revenues and components of claims that are expenses must be recognised separately in the statement of financial performance. Components of premiums that are not revenues and components of claims that are not expenses must be recognised as changes in policy liabilities.

6.2 For products where the separation of premiums and claims into components is not practicable or the components cannot be reliably measured, premiums must be recognised as revenues and claims must be recognised as expenses.

COMMENTARY

6.2.1 A wide variety of products are offered by life insurers — risk products, investment products and numerous hybrids of these two products.

6.2.2 Traditionally, life insurers have treated all premiums as revenues and essentially all claims as expenses. However, premiums may comprise amounts that give rise to:

(a) revenues that are earned by providing services, including the bearing of risks

(b) amounts that are akin to deposits and which qualify for recognition as liabilities.

6.2.3 Similarly, claims may comprise amounts that give rise to:

(a) expenses that are incurred in providing services, including the bearing of risks

(b) amounts that are akin to withdrawals from deposits and which qualify for recognition as reductions in liabilities.

6.2.4 The performance of a life insurer is best reflected when only revenues and expenses are recognised in the statement of financial performance. The inclusion of other types of flows limits the ability of users to assess the performance of a life insurer's operations relative to other entities or investments.

6.2.5 The hybrid nature of many products and the sometimes complex manner in which fees are levied on policyholders means that differentiating between the revenue and the liability components of premiums, and the expense and the liability components of claims, may be a difficult task and the costs involved may be significant. This is especially the case for products that are non-investment-linked. Notwithstanding the difficulties associated with reliably measuring the components of premiums and claims for products where the components can be reliably measured, the premiums and claims associated with those products are separately recognised as revenues, expenses and changes in policy liabilities for financial reporting purposes.

7 REINSURANCE

Substance of Reinsurance Contracts

STANDARD

7.1 Reinsurance contracts must be accounted for as reinsurance in accordance with paragraphs 7.3 and 7.4 when and only when they provide for the transfer of risk against loss or liability from the ceding insurer to the reinsurer.

7.2 When a contract does not, despite its form, provide for the transfer of risk against loss or liability from the ceding insurer to the reinsurer, it must not be accounted for as reinsurance. The premium paid by the ceding insurer must be recognised as:

(a) an asset by the ceding insurer

(b) a liability by the reinsurer.

COMMENTARY

7.2.1 A contract is not accounted for as reinsurance, regardless of its form, unless it provides for the transfer of risk from the ceding insurer to the reinsurer. This means, for example, that the amounts paid and received under a contract which provides for only an immaterial transfer of risk will be recognised as an asset by the ceding insurer and as a liability by the reinsurer. If a contract does not transfer risks from the ceding insurer to the reinsurer, a contract does not give rise to premiums that are revenues and claims that are expenses.

Reporting by Direct Insurers

STANDARD

7.3 A ceding insurer must recognise:

(a) premiums ceded to reinsurers as reinsurance expenses

(b) claim recoveries and commissions from reinsurers as revenues

(c) claims recoveries and other inflows not yet received from a reinsurer as an asset.

COMMENTARY

7.3.1 Life insurers may reinsure some of their business. The direct life insurer remains responsible for the total amount of successful claims of policyholders and through reinsurance arrangements may be entitled to recover amounts relating to some of those claims.

7.3.2 Reinsurance contracts are considered to be separate transactions from the original life insurance policies and therefore give rise to separately recognisable amounts. The direct insurer recognises the gross amount of premiums received in accordance with paragraphs 6.1 and 6.2 and, where portions of the policies are reinsured, the ceded premiums are recognised as expenses. Any recoveries from reinsurers are recognised as revenues by the direct life insurer. Consistent with this approach, the gross amount of policy liabilities is recognised as a liability and claim recoveries not yet received from a reinsurer are recognised as a receivable by the direct insurer.

Reporting by Reinsurers

STANDARD

7.4 Inwards reinsurance premiums and outwards reinsurance claims must be recognised by the accepting reinsurer as for premiums and claims in accordance with paragraphs 6.1 and 6.2. Policy liabilities assumed must be recognised as a liability by the accepting reinsurer in accordance with section 9.

COMMENTARY

7.4.1 From the perspective of the reinsurer, reinsurance premiums accepted are recognised in the same way as the direct life insurer treats the acceptance of direct premiums. Correspondingly, claims paid and payable to direct insurers are recognised as expenses by the reinsurer. Consistent with these treatments, policy liabilities assumed are recognised as a liability by the accepting reinsurer.

8 INVESTMENT REVENUES

STANDARD

8.1 Returns on all investments controlled by a life insurer must be recognised as revenues.

COMMENTARY

8.1.1 Interest, dividends, realised and unrealised capital gains and other returns on all the investments under the life insurer's control are revenues of the life insurer. This is the case whether the source of the investment returns are investments relating to premium revenues from policyholders, investments relating to inflows of deposits from policyholders or investments relating to funds received from shareholders. This treatment is consistent with the view that the life insurer controls the investments relating to both policyholders and shareholders and is responsible for investing them with the aim of maximising returns within risk constraints. In regard to the investments relating to policyholders, the life insurer has contracts with policyholders to pass on some or all of the investment returns based on the terms of the contracts. The investment returns related to the investments of both policyholders and shareholders are investment returns of the life insurer and, in turn, the life insurer will use those returns to meet its contractual obligations to policyholders.

9 POLICY LIABILITIES

Present Value and Best Estimates

STANDARD

9.1 Obligations arising from life insurance policies (policy liabilities) must be recognised as liabilities and must be measured at each reporting date as:

(a) the net present value of future receipts from and payments to policyholders, including participating benefits, allowing for the possibility of discontinuance before the end of policy contract periods, plus planned margins of revenues over expenses relating to services yet to be provided to policyholders, on the basis of assumptions that are best estimates; or

(b) where the result would not be materially different from the application of paragraph 9.1 (a), the accumulated benefits to policyholders after allowing for the portion of acquisition costs expected to be recouped.

COMMENTARY

9.1.1 The participating benefits component of policy liabilities includes previously vested benefits and future supportable bonuses. In addition to policy liabilities, there may be other liabilities that relate to participating policyholders. Policy benefits attributable to participating policyholders that are not yet vested with specific policyholders are recognised as liabilities. These are further discussed in section 11.

9.1.2 Premiums are generally received in advance of the provision of services to policyholders, including the payment of claims. In return for premiums, life insurers provide services, including the acceptance of risks, sometimes over long periods. Entering into a life insurance policy is considered to be the event that gives rise to future benefits and present obligations under a policy.

9.1.3 Where there are a number of variables relating to future uncertainties, a net present value approach to measuring policy liabilities is likely to provide the most appropriate measurement basis. The obligations under these more complex policies are generally measured as the present value of the expected inflows, such as premiums and fees, and outflows, such as claims and other expenses, based on assumptions relating to whole populations of policyholders, and taking into account applicable taxation.

9.1.4 An accumulation approach involves accruing the entitlements in policyholders' records at the reporting date. For example, in the case of an investment-linked policy, the life insurer could accrue the accumulated returns on the amount invested. If the fees expected to be charged by the life insurer to the policyholder in each future reporting period are expected to equal or exceed any expenses incurred by the life insurer, the policy liability calculated under the accumulation approach would not be materially different from that obtained using the approach in paragraph 9.1(a).

9.1.5 The ultimate cost of meeting claims under many life insurance policies depends on the frequency of occurrence of particular future events such as death and surrender and other factors such as the future levels of investment returns, which are taken into account in setting discount rates. Assumptions need to be made about these future events. In order to ensure that policy liabilities are measured reliably, such assumptions need to be "best estimates".

9.1.6 Best estimate assumptions used in determining the present value of policy liabilities are made on the basis of the assets available to the life insurer at the reporting date and do not include any allowance for future contributions by owners and other funds which may be provided in the future to support the business.

9.1.7 Measurement under paragraphs 9.1(a) and (b) should be undertaken in accordance with actuarial guidelines and standards issued by the New Zealand Society of Actuaries.

Acquisition Costs

COMMENTARY

9.1.8 Life insurance policies written in one reporting period often give rise to benefits to the life insurer in subsequent reporting periods, such as future management fees and surrender penalties. Therefore, there are future benefits associated with the costs of acquiring life insurance policies, and such costs are often substantial.

9.1.9 Where relevant, in most industries, acquisition costs are added to the carrying amounts of the assets acquired and subsequently amortised. In the life insurance industry, there is no reliable measure of the probable future economic benefits that will arise from acquisition costs. This is largely because of the uncertainty surrounding the continuance or surrender of particular policies. In practice, acquisition costs are usually recognised as expenses in the period in which they are incurred. This is generally offset by identifying a portion of the planned margins included in policy liabilities as relating to the recovery of acquisition costs. The most useful and reliable information available about the acquisition costs that will give rise to future economic benefits is the amount of future charges for acquisition costs identified as part of the process of determining policy liabilities.

Recognition of Planned Margins as Revenues

STANDARD

9.2 Planned margins of revenues over expenses must be recognised in the statement of financial performance over the reporting periods during which the services to which those margins relate are provided to policyholders and the revenues relating to those services are received.

COMMENTARY

9.2.1 In setting premium rates, life insurers will include planned margins of revenues over expenses. As noted in paragraph 9.1.2, premiums are generally received in advance of the provision of services to policyholders.

9.2.2 In this Standard, planned margins are recognised in the statement of financial performance when and only when the life insurer has performed the services necessary to establish a valid claim to those margins and has received the revenues relating to those services. To ensure that planned margins are recognised during the reporting period in which the relevant services are provided, policy liabilities include a component relating to those margins. These margins are then "released" based on one or more factors or "profit carriers" which correspond to the performance of services and the earning of the margins. In relation to investment-linked business, the profit carrier might be maintenance expenses. In relation to many risk products, the profit carrier might be premiums or claims.

Differences Between Actual and Assumed Experience

STANDARD

9.3 Except in relation to investment earnings rate assumptions for participating business, the effect of changes in policy liabilities resulting from a difference between actual and assumed experience determined during the reporting period must be recognised in the statement of financial performance as revenues or expenses in the reporting period in which the changes occur.

COMMENTARY

9.3.1 The assumed patterns and frequencies of events used in determining policy liabilities are compared with actual events in each reporting period to assess their accuracy. The effects of differences between actual and assumed experience represents decreases or increases in the expected payments to policyholders and are revenues or expenses of the reporting period in which the differences occur. For example, where the assumed costs of death claims under a renewable term life product line are greater than the actual costs for a reporting period, a revenue equal to the difference is recognised in the statement of financial performance for the current reporting period.

9.3.2 The recognition of the net amount of changes in policy liabilities resulting from a difference between actual and assumed experience identified during the reporting period as a revenue or an expense is consistent with the use of assumptions that are best estimates as at each reporting date.

Changes to Underlying Assumptions

STANDARD

9.4 Assumptions used for measuring policy liabilities must be reviewed for each reporting period. Where the review leads to changes in assumptions, with the exception of new business, the changes must be deemed to occur at the reporting date.

COMMENTARY

9.4.1 Assumptions used for measuring new business may be deemed to have occurred at the beginning of the reporting period, or at the date of the commencement of new business or at the end of the reporting period.

9.4.2 In preparing interim financial statements the reporting date is the interim reporting date. Accordingly, changes in assumptions are deemed to occur at the interim reporting date.

STANDARD

9.5 The financial effects of changes to the assumptions underlying the measurement of policy liabilities made during the reporting period must be

recognised in the statement of financial performance over the future reporting periods during which services are provided to policyholders, except that:

(a) any estimated excess of the present value of future expenses over the present value of future revenues for a group of related products arising during the reporting period must be recognised as an expense of the reporting period

(b) the reversal of an expense previously recognised in accordance with sub-paragraph 9.5(a) must be recognised as a revenue of the reporting period in which the reversal of the loss is recognised

(c) the effects of a change to assumed discount rates caused by changes in investment market conditions must be recognised as a revenue or an expense of the reporting period in which the change occurs

(d) calculation errors and similar errors must be recognised as revenues or expenses in the reporting period in which they are identified.

COMMENTARY

9.5.1 The assumptions underlying the measurement of policy liabilities are reviewed at each reporting date. Based on past experience and revised expectations about the future, it may become apparent that particular assumptions are not consistent with likely future experience and need to be changed. Such changes are effectively a reassessment of the likely patterns and frequencies of future events. The normal revision of assumptions is not considered to be an error.

9.5.2 Apart from the circumstances identified in paragraph 9.5, changes to underlying assumptions are effectively recognised over future reporting periods by adjusting the planned margins included in policy liabilities. If the effect of a changed assumption is a decrease in the present value of present obligations to policyholders, the planned margin is increased. If the effect is an increase in the present value of obligations to policyholders, the planned margin is reduced. The overall amount of policy liabilities is not affected by these changes to underlying assumptions, as long as the planned margin of revenues over expenses is not eliminated.

Losses on Groups of Related Products

COMMENTARY

9.5.3 Situations may arise where the present value of the planned margin of revenues over expenses for a group of related products will be adjusted as a result of changing underlying assumptions to the extent that the planned margin is eliminated and becomes a planned loss. That is, the present value of estimated future expenses for a group of related products exceeds the present value of estimated future revenues. In such circumstances, the excess of the present value of expenses over revenues arising during the reporting period is recognised in the statement of financial performance in the reporting period in which the assessment

is made. The loss reflects a higher present obligation due to adverse claims, which are now expected in future periods. Whilst the claims giving rise to the loss are yet to occur, this treatment is justified on the basis that entering into life insurance policies is an event that gives rise to a present obligation to meet the expected future claims.

9.5.4 A group of related products would be products that have substantially the same contractual terms and were priced on the basis of substantially the same assumptions.

Changes to Discount Rates

COMMENTARY

9.5.5 As with other assumptions, the discount rates used in determining policy liabilities are reviewed at each reporting date. Discount rates are based on currently expected rates of return on the assets supporting policy liabilities (refer to paragraph 9.6). However, unlike other assumptions, the effects of a change to assumed discount rates caused by changes in investment market conditions are recognised in the reporting period in which the change is made. For a life insurer with a typical spread of investments, if market rates of return fall investment values generally rise and the resulting increases in investment values are recognised as revenues in the reporting period in which they occur. Where the discount rates are adjusted in line with such falls in market rates, policy liabilities will increase and an expense will be recognised, having an offsetting (but not usually matching) effect on the increased investment values.

9.5.6 In relation to participating business (which is discussed at section 11), the effect of a change to the assumptions about discount rates, explained in paragraph 9.5.5, is a result of adjusting the best estimate of policy liabilities, including future participating benefits. For example, if market rates of return rise investment values generally fall and the resulting decreases in investment values are recognised as an expense in the reporting period in which they occur. The fall in investment values will clearly impact on the ability of the life insurer to support future participating benefits. These are likely to be reduced, with an offsetting effect on the reduced investment values. The effect of an adjustment on the best estimate of future participating benefits included as a component of policy liabilities is the same as an adjustment of policy liabilities in the case of non-participating business.

Discount Rates

STANDARD

9.6 The discount rates used in determining policy liabilities must be based on expected average market returns on investments supporting policy liabilities. Where appropriate, the discount rates must be adjusted for factors such as tax.

COMMENTARY

9.6.1 Among the key assumptions underlying the present value measurement of policy liabilities are the discount rates used in discounting expected future cash flows. The most relevant amount of policy liabilities is the amount which is required as at the reporting date to meet a life insurer's policy obligations when they fall due. If policy liabilities are to represent expected cash flows, the discount rates used need to be based on the average returns on investments that are currently expected to arise and will contribute to discharging policy liabilities. The discount rates would relate to the total expected yields on investments and would therefore comprise what are sometimes described as income and capital gains.

10 OTHER LIABILITIES

STANDARD

10.1 Other liabilities must be measured at net present values as at reporting date. Any changes in the net present values must be recognised in the statement of financial performance as revenues or expenses in the reporting period in which the changes occur.

COMMENTARY

10.1.1 This Standard requires that policy liabilities are measured at net present values and assets are measured at net market values. It is consistent to also measure other liabilities, including subordinated debt, at net present values using discount rates that reflect current market conditions for the liabilities concerned. That is, for example, a changed market yield for a long-term debt would result in a changed amount being recognised as a liability in the statement of financial position and in a revenue or an expense being recognised in the statement of financial performance. It should be noted that where other liabilities are immaterial, they could be measured on a cost basis without contravening this Standard.

11 PARTICIPATING BENEFITS

STANDARD

11.1 Except for transfers from unvested policyholder benefits liabilities, participating benefits vested in policyholders in relation to the reporting period must be recognised as expenses for the reporting period. Such benefits which remain payable as at the reporting date must be recognised as a component of policy liabilities.

11.2 Participating benefits that have been allocated in relation to the reporting period to participating policyholders generally, but that have not yet vested in specific policyholders, must be recognised as expenses for

the reporting period. Amounts that have been allocated to participating policy-holders generally, but that have not vested in specific policyholders as at the reporting date, must be recognised as unvested policyholder benefits liabilities.

COMMENTARY

11.2.1 Some life insurers sell participating business. Participating policyholders are generally eligible to receive the same types of benefits as other policyholders and, in addition, are entitled to participate in the profits relating to participating business. For example, a participating policyholder may receive a low contractually determined rate of return on savings together with term life cover and, in addition, receive benefits that depend on the investment performance of the pool of assets associated with participating policies and on the risk experience of participating policyholders. These additional benefits are often called bonuses and are at the discretion of the life insurer. In some reporting periods the life insurer may withhold a portion of the "profits" from the pool of participating business and recognise these "profits" as unvested policyholder benefits liabilities. In other reporting periods the life insurer may "top up" the vested benefits to participating policyholders. Such vesting of benefits is often done to provide a reasonably level vesting of benefits over time, despite volatility in periodic profits from participating business.

11.2.2 It is sometimes argued that the discretionary nature of participating benefits means that they should be treated as appropriations of profit in the same way as dividends to shareholders. Because policy liabilities relating to all types of policyholders are recognised as liabilities, it is appropriate for the participating benefits vested in relation to the reporting period, other than transfers from unvested policyholder benefits liabilities, to be recognised as expenses of the reporting period.

11.2.3 Mutual life insurers are effectively owned by their policyholder members. Nevertheless, the mutual life insurer also has obligations to its policyholders. These obligations are classified as policy liabilities. Benefits vested in a mutual life insurer's policyholders, other than transfers from unvested policyholder benefits liabilities, are also to be recognised as expenses in the reporting period in which they are vested.

11.2.4 For financial reporting purposes, participating benefits vested in policy-holders in a reporting period but not yet paid are included in policy liabilities and are measured at net present values. In the case of investment account participating business this may be approximately the same as the amount actually allocated to policyholder accounts. In the case of traditional participating business, there may be a significant difference between the net present value and the face value of the amount vested in policyholders. The net present value is relevant for financial reporting purposes because it is the best estimate of the net

present value of the amount that the life insurer expects to pay out in the future using information of experience up to the reporting date.

11.2.5 Where a life insurer "tops up" the vested benefits from previously recognised unvested policyholder benefits liabilities, a transfer between liabilities is recognised. If a life insurer tops up the vested benefits for participating policyholders other than from unvested policyholder benefits liabilities, the amount of the "top up" is recognised as an expense of the reporting period in which the additional benefits are vested.

12 ASSETS

Measurement

STANDARD

12.1 Assets of a life insurer must be measured at net market values as at reporting date. Any changes in the net market values must be recognised in the statement of financial performance as revenues or expenses in the reporting period in which the changes occur. For assets without active and liquid markets, the methods used to determine their net market values must be disclosed.

COMMENTARY

12.1.1 The assets of a life insurer will typically comprise:

(a) investments, including investments in subsidiaries

(b) operating assets, such as fixtures and fittings

(c) accounts receivable

(d) cash.

12.1.2 In determining net market values of investments, reference is made to the market that provides the most reliable information, which is likely to be the market in which the investment is normally traded. In addition, whilst investments are often managed in the context of portfolios, they are nonetheless measured individually.

12.1.3 For many assets, such as equity securities of major listed companies, quoted market prices provide a reliable measure of net market value at reporting date. However, in some cases, it may be difficult to reliably measure the net market value of an asset. For example, in the case of a shareholding in a private company there may not be an active and liquid market for the shares. In such circumstances, the life insurer would make its best estimate of the net market value of that asset, taking into account all available information. In the case of material classes of assets, disclosure of the methods used in determining the net market values are relevant to users of the financial statements in assessing the financial performance and financial position of the life insurer.

12.1.4 In accordance with paragraph 12.1, a parent entity that is a life insurer would classify its interests in subsidiaries, including any life insurer subsidiaries, as investments and measure them at net market value.

12.1.5 It is sometimes argued that a distinction should be made between investment and operating assets of life insurers for measurement purposes. Under this view, investments would be measured at net market values whilst operating assets would be measured in accordance with SSAP-28: *Accounting for Fixed Assets* and SSAP-3: *Accounting for Depreciation*.

12.1.6 Any distinction between investment and operating assets is arbitrary because all assets of a life insurer contribute to generating returns to satisfy policyholder and shareholder expectations. The use of net market values and the recognition of all changes in values as revenues and expenses provide relevant information to users about the resources available to policyholders and shareholders and the life insurer's performance in deploying those assets. Where operating assets are immaterial, they could be measured on a cost basis without contravening this Standard.

12.1.7 The valuation of land and buildings is to be undertaken either by an independent valuer, or where a life insurer has in its employ a qualified valuer, by an internal valuer, so long as the basis of valuation has been subject to review by an independent valuer. Both independent and internal valuers are to hold a recognised professional qualification and have experience in the location and category of asset being valued.

Recognition

STANDARD

12.2 A life insurer must not recognise the excess of its own embedded value over its recognised net assets as an asset.

COMMENTARY

12.2.1 Although section 5 requires that a life insurer recognise a subsidiary at market value in both the "parent" and group financial statements, this Standard prohibits a life insurer from recognising the excess of its own embedded value over its other recognised net assets in its financial statements.

13 IMPUTED INFLOWS AND OUTFLOWS

STANDARD

13.1 Subject to paragraph 18.3, a life insurer must recognise imputed inflows and outflows as revenues and expenses when, and only when, such imputed flows relate to transactions with external entities.

COMMENTARY

13.1.1 Life insurers often impute inflows and outflows to different classes of policyholders in order to help ensure that they are treated equitably. For example, a life insurer may own the buildings that it occupies. The funds of a particular group of policyholders are used to acquire and operate such buildings whilst a wider group of policyholders and shareholders may benefit from the use of the buildings. In the owner-occupied building example, the life insurer imputes an inflow of rent income to the policyholders whose funds are used to acquire and operate the buildings and imputes an outflow of rent cost to the other policyholders and to shareholders.

13.1.2 In cases where there are no transactions with external entities, such as with owner-occupied buildings, the life insurer is dealing with itself. There is no transaction or other past event that gives rise to a revenue or an expense. Any inflows and outflows imputed for internal management purposes would be eliminated in preparing external financial statements except in relation to the disaggregated disclosures required by paragraph 18.2.

13.1.3 In some cases, life insurers impute inflows and outflows where external entities are involved. For example, life insurers often lend funds to their employees at concessional rates of interest with the funds being provided by a particular group of policyholders, whilst other policyholders and any shareholders benefit from the services provided by those employees. Because external parties are involved, such imputed inflows and outflows are recognised as revenues and expenses when they can be reliably measured.

14 INCOME TAX

Application of Tax Standard

STANDARD

14.1 Life insurers must account for income tax in accordance with SSAP-12: *Accounting for Income Tax* except that:

(a) tax assets and liabilities must be measured at present values; and

(b) disclosures about permanent differences or a reconciliation between income tax expense and income tax calculated at the current rate on the operating result are not required; and

(c) the comprehensive basis for tax effect accounting must be used.

COMMENTARY

14.1.1 It is important for life insurers to maintain equity between existing policyholders and between policyholders over time. This is reflected in the financial statements through the use of current value methods of measurement.

14.1.2 Liabilities are generally measured at net present values and assets are measured at net market values, which reflect net present values. It is consistent for life insurers to also measure tax assets and liabilities at present values. Tax assets and liabilities will effectively be at present values where they are determined on the basis of tax effects on liabilities and assets that are measured at net present values or net market values. However, the timing of the relevant tax cash flows may need to be examined to determine whether any adjustments are needed. In addition, the discount rates used to determine the present values of tax assets and liabilities may need to be different from the rates used for other assets and liabilities because the risks pertaining to tax-related cash flows are different from the risks associated with other cash flows.

14.1.3 SSAP-12 requires a reconciliation between income tax expense in the statement of financial performance and income tax calculated at the current rate applied to the operating result. The income tax payable by a life insurer is determined on a basis that is not derived from its operating results. Accordingly, detailed disclosures about the nature and extent of any permanent differences are not useful to users of the financial statements.

14.1.4 SSAP-12 favours the use of the comprehensive basis of tax effect accounting but permits the partial basis where certain criteria are met. The use of partial tax effect accounting is often viewed as a substitute for the use of the comprehensive basis in conjunction with discounting, as both have the effect of reducing the amounts of tax assets and liabilities recognised. The application of both the partial method and discounting would give rise to distorted amounts of tax assets and liabilities and this Standard requires the comprehensive basis to be applied by life insurers in conjunction with discounting.

Disclosure

STANDARD

14.2 The financial statements must include a brief description of the income tax regime applying to the life insurer and disclose the basis on which the carrying amounts of tax assets and liabilities have been determined.

COMMENTARY

14.2.1 Life insurance activities are taxed in various ways, usually dependent on the nature of the product involved. The forms and rates of tax are often different from those applying in other industries and information about the tax regime under which each life insurer operates is useful to users of financial reports.

Policyholder Credit Account

STANDARD

14.3 The notes to the financial statements must disclose the movements in, and balance of, the Policyholder Credit Account.

15 FINANCIAL PERFORMANCE DISCLOSURES

STANDARD

15.1 The following revenues and related explanations must be disclosed:

(a) premium revenue

(b) the accounting policy adopted in recognising premium revenue

(c) inwards reinsurance revenues

(d) investment revenue, showing separately revenue from:

- **(i) equity securities**
- **(ii) debt securities**
- **(iii) properties**
- **(iv) other**

(e) revenue arising from the recognition of a deficiency of the net market values of interests in subsidiaries (or other entities) over the net amount of subsidiaries' (or other entities') assets and liabilities, in accordance with paragraph 5.4

(f) other revenue.

COMMENTARY

15.1.1 In accordance with the principles embodied in this Standard, with the exception of premium revenue recognised in accordance with section 6.1, all revenues are to be recognised and disclosed before the effects of any transfers to or from policy liabilities. Disclosure of the effects of transfers to and from policy liabilities is required by section 15.5.

15.1.2 Investment revenues are shown in four categories, and the amount in each category would potentially include amounts received, amounts receivable and realised and unrealised gains and losses relating to the reporting period. That is, for example, the category "investment revenues from equity securities" would include dividends received and receivable relating to the reporting period, realised gains and losses from trading during the reporting period and unrealised gains and losses from holding equity securities during the reporting period.

STANDARD

15.2 The following expenses and related explanations must be disclosed:

(a) outwards reinsurance expense

(b) operating expenses, showing separately:

- **(i) claims expense**
- **(ii) policy acquisition expenses, separated into material components including commission**
- **(iii) policy maintenance expenses**
- **(iv) investment management expenses**
- **(v) other**

(c) the accounting policy adopted in recognising claims expense

(d) the basis for the apportionment of operating expenses between policy acquisition, policy maintenance and investment management expenses

(e) any expense arising from the recognition of a deficiency of the net market values of interests in subsidiaries (or other entities) over the net amount of subsidiaries' (or other entities') assets and liabilities, in accordance with paragraph 5.4.

COMMENTARY

15.2.1 In accordance with the principles embodied in this Standard, with the exception of claims expense recognised in accordance with paragraph 6.1, all expenses are to be recognised and disclosed before the effects of any transfers to or from policy liabilities. Disclosure of the effects of transfers to and from policy liabilities is required by section 15.5.

STANDARD

15.3 Where any premiums and any claims are separated into their revenue, expense and change in liability components in accordance with paragraph 6.1, total premiums and total claims must be disclosed.

COMMENTARY

15.3.1 The mix of products written by a life insurer will vary between life insurers. In addition, different life insurers will find that the separation of premiums and claims into their components is practicable for different products. Comparability between life insurers is enhanced by the disclosure of total premiums and total claims.

STANDARD

15.4 Where a profit is recognised at the inception of a group of policies, the revenues and expenses associated with that group of related products must be disclosed in the reporting period in which those policies were written.

COMMENTARY

15.4.1 It is expected that profit will be recognised at the inception of a policy only on rare occasions. It is considered that this profit would be so infrequent that it should be disclosed.

STANDARD

15.5 The following components of surplus after income tax expense must be shown:

(a) surplus related to movements in policy liabilities, separated between:

- **(i) planned margins of revenues over expenses**
- **(ii) the difference between actual and assumed experience**
- **(iii) the effects of changes to underlying assumptions**

  - **(iv) loss recognition on groups of related products or reversal of previously recognised losses**
  - **(v) other movements, separated into material components**
- **(b) investment earnings on assets in excess of policy liabilities**
- **(c) other items, separated into material components.**

Other Disclosures

COMMENTARY

15.5.1 "*Not Used*"

15.5.2 This Standard prescribes disclosure requirements specific to life insurance business. Other accounting standards prescribe disclosure requirements for all entities, including life insurers.

16 FINANCIAL POSITION DISCLOSURES

Assets

STANDARD

16.1 The following assets must be disclosed in the broad order of their liquidity:

- **(a) investments, showing separately:**
  - **(i) equity securities**
  - **(ii) debt securities**
  - **(iii) properties**
  - **(iv) other, by major class where applicable**
- **(b) operating assets**
- **(c) reinsurance recoveries receivable**
- **(d) any excess net market value asset recognised in accordance with paragraph 5.3, together with the components disaggregated by subsidiary, and explanations of:**
  - **(i) the factors giving rise to that asset; and**
  - **(ii) any changes in that asset from the previous reporting period.**

Liquidity Ranking

COMMENTARY

16.1.1 The presentation of assets and liabilities in the broad order of their liquidity is considered to be relevant to emphasise the importance of liquidity and solvency for life insurers. The current/non-current presentation of assets and liabilities is not considered to give rise to sufficiently useful information for users.

Investments

COMMENTARY

16.1.2 Disclosure about the different types of investments and investment revenues provide users with information that assists them in understanding the nature and extent of the risks and returns associated with the investments held by a life insurer. Accordingly, investments are shown in classes that reflect their underlying nature. For example, units held in a property trust are classified as a property investment.

16.1.3 Some types of land and buildings may be investments that are also used in the operation of the life insurance business. An example is office buildings owned and occupied by a life insurer. The predominant purpose in holding all types of land and buildings in the context of a life insurance business is the generation of investment returns. Accordingly, these assets are classified as investments.

Measurement Methods

COMMENTARY

16.1.4 Paragraph 12.1 requires assets to be measured at net market values as at reporting date, and that where assets are without active and liquid markets, the methods used to determine their net market values are to be disclosed.

Other Disclosures

COMMENTARY

16.1.5 This Standard requires minimum disclosures and it is likely that, in many cases, more extensive disclosures would be appropriate. For example, in relation to investment properties it may be useful to disclose separately the extent of holdings in the commercial/retail, industrial, rural, and residential sectors.

Restrictions on Assets

STANDARD

16.2 Restrictions attaching to assets held for the benefit of policyholders must be disclosed.

COMMENTARY

16.2.1 There are a number of restrictions on the use of assets invested for policyholders in life funds. It is important that these restrictions be disclosed so that users of the financial report can assess their impact.

Liabilities

STANDARD

16.3 Policy liabilities, unvested policyholder benefits liabilities and other liabilities, classified by nature, must be disclosed in the broad order of

their liquidity. The following components of policy liabilities must also be disclosed:

(a) future policy benefits, including participating benefits

(b) balance of future expenses

(c) planned margins of revenues over expenses

(d) future charges for acquisition costs

(e) balance of future revenues

(f) other items, separated into material components.

Acquisition Costs

COMMENTARY

16.3.1 In the life insurance industry, unlike other industries, acquisition costs are not recognised as an asset because there is no reliable measure of the probable future economic benefits that will arise from actual acquisition costs. In practice, acquisition costs are usually recognised as expenses in the reporting period in which they are incurred. This is generally offset by identifying a portion of the planned margins included in policy liabilities as relating to the recovery of acquisition costs. The most useful and reliable information available about the acquisition costs that will give rise to future economic benefits is the amount of future charges for acquisition costs identified as part of the process of determining policy liabilities. Disclosure of this amount is required under paragraph 16.3(d).

Assured Returns of Funds Invested

STANDARD

16.4 The amount of policy liabilities which relates to assured returns of funds invested must be disclosed.

COMMENTARY

16.4.1 Many life insurers sell life insurance policies that provide some form of assurance about the return of funds invested. It is useful for users of life insurers' financial statements to have information about the extent of such guarantees or assurances, since they involve the life insurer bearing investment risks on behalf of policyholders.

Equity

STANDARD

16.5 The following components of equity must be disclosed:

(a) retained profits wholly attributable to shareholders

(b) retained profits where the allocation between participating policyholders and shareholders cannot be determined.

COMMENTARY

16.5.1 Information about the different components of retained profits is useful in meeting the accountability obligations of the life insurer for the whole business and in showing the relative positions of the major stakeholders.

16.5.2 A life insurer that has sold participating life insurance business may have "retained profits" generated from that business. These "retained profits" are liabilities which are disclosed separately from policy liabilities in accordance with paragraph 16.3. In foreign life insurance operations, retained profits may exist which have yet to be allocated between policyholders and shareholders. Such retained profits should be separately disclosed.

Solvency Information

STANDARD

16.6 The amount of equity retained as solvency reserves and the basis of establishing the amount must be disclosed. A group must disclose the solvency position of each life insurer in the group.

16.6.1 "*Not Used*"

Managed Funds and Other Fiduciary Activities

STANDARD

16.7 The nature and amount of the life insurer's activities relating to managed funds and trust activities, and whether arrangements exist to ensure that such activities are managed independently from its other activities, must be disclosed.

17 ACTUARIAL INFORMATION

STANDARD

17.1 The following must be disclosed in notes to the financial statements:

(a) if other than the reporting date, the effective date of the actuarial report on policy liabilities and solvency reserves

(b) the name and qualifications of the actuary

(c) whether the amount of policy liabilities has been determined in accordance with the standards of the New Zealand Society of Actuaries

(d) whether the actuary is satisfied as to the accuracy of the data from which the amount of policy liabilities has been determined.

Disclosure of Assumptions

STANDARD

17.2 A summary of the key assumptions used in determining policy liabilities must be disclosed in notes to the financial statements, including:

(a) discount rates, asset mix, and inflation rates

(b) profit carriers used for each major product group

(c) future maintenance and investment management expenses, the rate of inflation applicable to them and any automatic indexation of benefits and premiums

(d) rates of taxation

(e) mortality and morbidity, by reference to the identity of the tables

(f) rates of discontinuance

(g) the basis of calculating surrender values

(h) rates of growth of unit prices in respect of unit-linked benefits

(i) rates of future supportable participating benefits

(j) the crediting policy adopted in determining future supportable participating benefits and how it compares with the life insurer's actual practice.

18 DISAGGREGATED INFORMATION

STANDARD

18.1 "*Not Used*"

18.1.1 "*Not Used*"

Investment-linked and Non-investment-linked Business

STANDARD

18.2 This Standard requires disclosure of disaggregated information as between those amounts relating to investment-linked business and those relating to non-investment-linked business. The following must be disclosed:

(a) investment assets

(b) other assets

(c) policy liabilities

(d) liabilities other than policy liabilities

(e) retained profits, showing the amount directly attributable to shareholders and other retained profits

(f) premium revenue

(g) investment revenue

(h) claims expense

(i) other operating expenses

(j) investment revenues paid or allocated to policyholders

(k) operating surplus (deficit) before tax

(l) operating surplus (deficit) after tax.

COMMENTARY

18.2.1 The risks and potential rewards for a life insurer differ substantially as between investment-linked business and non-investment-linked business. Accordingly, disaggregated information about these is considered to be useful in assessing the performance and financial position of a life insurer.

Geographical Segments

COMMENTARY

18.2.2 Further disaggregated information may be required by SSAP-23: *Financial Reporting for Segments.*

Imputed Inflows and Outflows

STANDARD

18.3 Disaggregated information must include all imputed inflows and outflows as revenues and expenses where they can be reliably measured.

COMMENTARY

18.3.1 As discussed in paragraph 13.1.1, life insurers often impute inflows and outflows to different classes of policyholders and shareholders to help ensure that they are treated equitably. Whereas, in relation to the statement of financial performance and statement of financial position, paragraph 13.1 only permits the recognition of imputed inflows and outflows relating to transactions with external parties, paragraph 18.3 requires all imputed inflows and outflows to be included in the disaggregated information to reflect the performance of each segment of the life insurer.

19 COMPARATIVE INFORMATION

STANDARD

19.1 Comparative figures for the prior period shall be given for all items in the financial statements in accordance with FRS-2: *Presentation of Financial Reports,* except for:

(a) the financial statements of a life insurer or the parent entity of a group containing a life insurer for the first reporting period to which this Standard applies, if impracticable; or

(b) the first consolidated financial statements of a life insurer after it becomes a parent entity; or

(c) the first consolidated financial statements of a non-life insurer after it becomes a parent of a life insurer.

20 TRANSITIONAL PROVISIONS

STANDARD

20.1 Any revenue or expense adjustment made by an entity in complying with the requirements of this Standard for the first time, shall be recognised in the statement of movements in equity as an adjustment against equity at the beginning of the period in which the adjustment is made.

20.2 All premiums and claims may be disclosed as if they are all revenues and expenses until the reporting period ending on or after 31 December 2001.

COMMENTARY

20.2.1 The transitional provision affects the recognition requirements of paragraphs 6.1 and 6.2, and the disclosure requirements of paragraphs 15.1a), 15.2(b)(i) and 15.3.

STANDARD

20.3 Any asset revaluation reserve recognised in the financial statements of a life insurer prior to the application of this Standard must be reclassified within equity. The amount reclassified shall not be taken to the statement of financial performance nor recognised in the statement of movements in equity.

21 DEFINITIONS

STANDARD

21.1 In this Standard:

acquisition costs **means the fixed and variable costs of acquiring new business, including commissions and similar distribution costs, and costs of accepting, issuing and initially recording policies**

appraisal value **means the embedded value of a life insurer together with the present value of expected profits from future new business**

assets **means future economic benefits or service potential controlled by the entity as a result of past transactions or other past events**

control **means the power to govern the financial and operating policies of another entity for the purpose of obtaining the benefits and/or assuming the risks normally associated with ownership**

embedded value **means the net present value of the shareholders' entitlements from existing assets and future cash flows from life insurance policies in force at the reporting date**

***entity* means any legal, administrative, or fiduciary arrangement, organisational structure or other party**

***equity* means the residual interest in the assets of the entity after deduction of its liabilities**

***expenses* means consumptions or losses of future economic benefits or service potential in the form of reductions in assets or increases in liabilities of the entity, other than those relating to distributions to owners, that result in a decrease in equity during the reporting period**

***financial statements* means the statements prepared by an entity to communicate information about its financial performance, financial position and cash flows**

***general purpose financial reports* means financial reports which are intended to provide information to meet the needs of external users who are unable to require the preparation of special reports to meet their specific information needs**

***group* means an entity reporting that comprises an investor and each of its subsidiaries**

***investment* means an asset held by the entity for the accretion of wealth by way of revenues such as interest, royalties, dividends, rentals and capital appreciation, but does not include operating assets**

***investment-linked business* means business for which the life insurer issues a contract where the benefit amount is directly linked to the market value of the investments held in the particular investment-linked fund**

***liabilities* means future sacrifices of economic benefits or service potential that the entity is presently obliged to make to other entities as a result of past transactions or other past events**

***life fund* means a Life Insurance Fund under the Life Insurance Act 1908**

***life insurance business* means all business conducted by a life insurer**

***life insurer* means an entity operating under the *Life Insurance Act 1908* and similar entities operating outside New Zealand**

***net market value* means the amount which could be expected to be received from the disposal of an asset in an orderly market after deducting costs expected to be incurred in realising the proceeds of such a disposal**

***non-investment-linked business* means life insurance business other than investment-linked business**

***non-participating business* means life insurance business that consists of the provision of non-participating benefits under life insurance policies**

participating business **means life insurance business that consists of the provision of participating benefits under life insurance policies**

recognised **means reported on, or incorporated in amounts reported on, the face of the statement of financial performance or of the statement of financial position (whether or not further disclosure of the item is made in notes)**

reporting date **means the end of the reporting period to which the financial report relates**

revenues **means inflows or other enhancements, or savings in outflows, of future economic benefits or service potential in the form of increases in assets or reductions in liabilities of the entity, other than those relating to contributions by owners, that result in an increase in equity during the reporting period**

subsidiary **means an entity (not being a joint venture entered into by the investor) that is controlled by the investor**

Acquisition Costs

COMMENTARY

21.1.1 Acquisition costs relate to the costs incurred in acquiring specific life insurance policies during the financial year. They do not include the general growth and development costs incurred by a life insurer.

APPENDIX 1

Comparison of FRS-34 with International and Australian Accounting Standards

Comparison with International Accounting Standards

As at the date of issuance of this Standard, the International Accounting Standards Committee has not issued a standard that corresponds with this Standard.

Comparison with Australian Accounting Standards

This Standard is the result of a joint project between New Zealand and Australia. Except for differences arising from the different regulatory regimes, the Standards arising from the project have identical requirements.

APPENDIX 2

Development of the Standard

This section does not form part of the Standard. The Standard was developed as a joint project by the Australian Accounting Standards Board and the New Zealand Financial Reporting Standards Board (the Boards). This section summarises the development of the Standard and the Boards' consideration of the key issues dealt with in the Standard.

1. The issue of the Standard follows consideration of the responses received on Proposed Accounting Standard ED-79/ED-73: *Life Insurance Business*, which was prepared by the Boards and released in July 1996.

Principal Features of ED-79/ED-73 Retained in the Standard

2. The Standard retains the basic structure and content of ED-79/ED-73. Assets are required to be measured at net market values and liabilities are required to be recognised at net present values. Premiums and claims are required to be separated into their revenue, expense and change in liability components except where this is not practicable.

Noteworthy Differences from ED-79/ED-73:

3. ED-79/ED-73 excluded life insurers that had been created for purposes other than writing life insurance business from the definition of a life insurer. The Standard applies to all life insurers.
4. ED-79/ED-73 proposed that policyholder retained profits be recognised as equity. The Standard requires that policyholder "retained profits" are classified as liabilities where they must be paid to participating policyholders, even if the timing and identification of the recipient policyholders is at the discretion of the life insurer.
5. ED-79/ED-73 was silent with respect to the treatment of a deficiency of the net market value of a life insurer's interest in a subsidiary over the net amount of that subsidiary's assets and liabilities. The Standard requires that a net deficiency is recognised as revenue.

Future Developments

6. ED-79/ED-73 was silent with respect to the treatment of the acquisition of a block of life insurance policies. The Boards intend to develop requirements for the recognition and measurement of a block of life insurance policies acquired by a life insurer as a separate project.

FRS-34