

IASC's Project on Insurance Accounting

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Overview

- ◆ What is IASC?
- ◆ IASC's Insurance Project

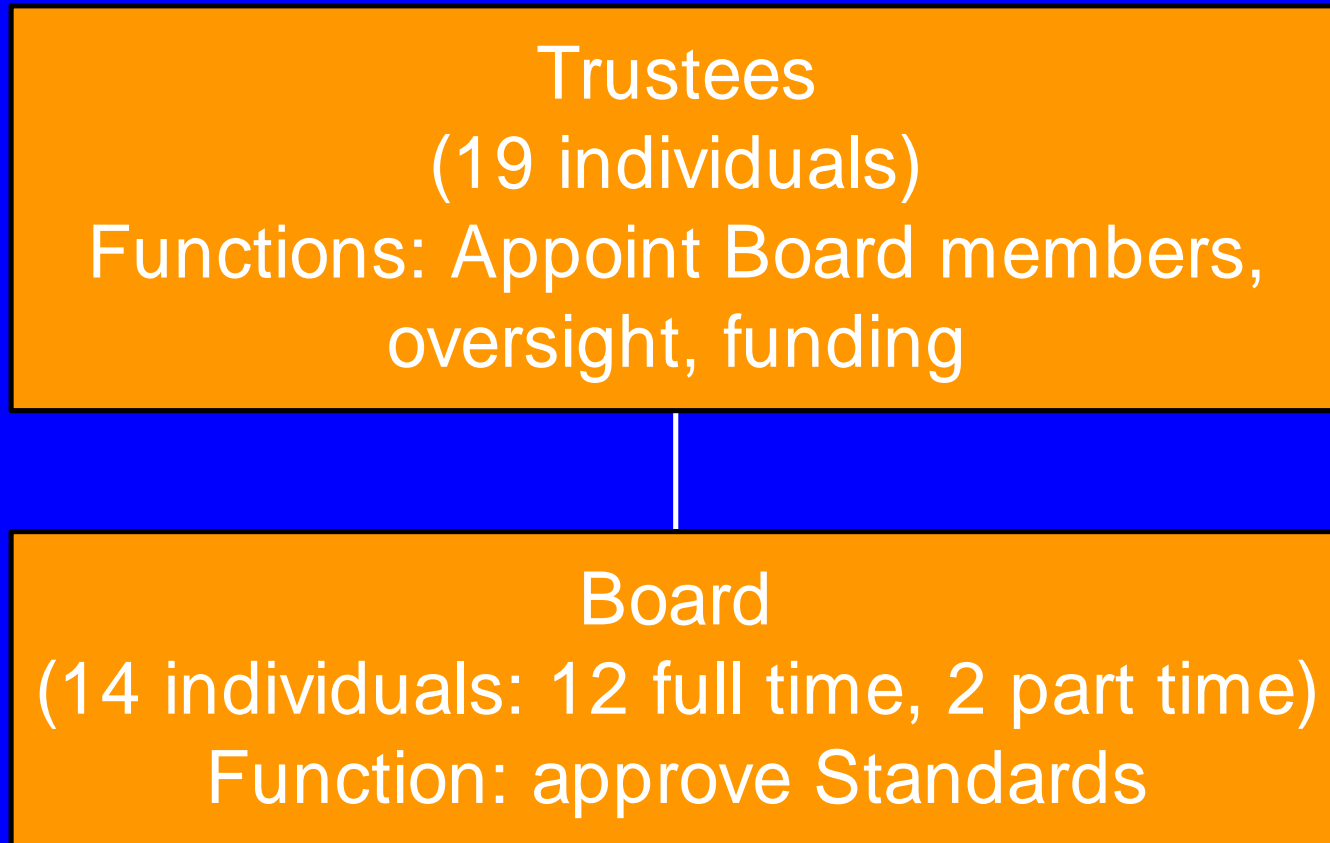


What is IASC?

- ◆ Members - 143 professional accountancy bodies in 104 countries
- ◆ IASC Board
 - 13 country members (professional accountancy bodies in 19 countries)
 - 3 co-opted members (financial analysts and financial executives)
 - Observers (IOSCO, EU, FASB, China)



New Structure for IASC



New Structure – Timetable

Nominating Committee to appoint first Trustees	Early 2000
Board approve structure	March 2000
IASC member bodies approve structure	May 2000
New Board starts	January 2001



Nominating Committee

- ◆ Chairmen of:
 - UK Financial Services Authority
 - US Securities and Exchange Commission
 - French Commission des Opérations de Bourse
 - Hong Kong Securities and Futures Commission
- ◆ President, The World Bank
- ◆ Chairman of the Supervisory Board, Siemens /
Deputy Chairman, German Accounting Standards
Committee
- ◆ Chief Executive Officer, Deloitte Touche
Tohmatsu



Core Standards

- ◆ Most stock exchanges already accept IAS for foreign issuers.
- ◆ Exceptions: Canada, Japan, USA
- ◆ Goal - IOSCO endorsement for cross-border listings
- ◆ SEC concept release – February 2000



G7 Declaration (1)

- ◆ “We call upon (...) IASC to finalise by early 1999 a proposal for a full range of internationally agreed accounting standards. IOSCO, IAIS, and the Basle Committee should complete a timely review of these standards.”

G7 Finance Ministers and Central Bank Governors, October 1998



G7 Declaration (2)

- ◆ We commit ourselves to endeavour to ensure that private sector institutions in our countries comply with these principles, standards and codes of best practice. We call upon (...) all countries which participate in global capital markets similarly to commit to comply with these internationally agreed codes and standards”



National Trends

- ◆ European Commission – IAS for listed companies?
- ◆ New laws - France, German, Belgium, Italy, Austria, Spain
- ◆ Harmonisation programmes (Australia, South Africa)
- ◆ Responses to the Asian crisis?
- ◆ Developing Countries



IASC Insurance Project - Provisional Timetable

- ◆ Steering Committee formed 1997
- ◆ Issues Paper * Nov 1999
- ◆ Comment deadline May 2000
- ◆ Draft Statement of Principles * 2000
- ◆ Exposure Draft 2001
- ◆ Final IAS 2002

* = Steering Committee document



Scope



Insurance **contracts** (or groups of contracts)

NOT

All aspects of accounting by
insurance **enterprises**



Why do we need a definition?

Insurance risk 	Insurance contract
No insurance risk 	Financial instrument



Insurance Contract (1)

- ◆ A contract under which one party (the **insurer**) accepts an insurance risk by agreeing with another party (the **policyholder**) to make payment if a specified uncertain future event occurs ...



Insurance Contract (2)

- ◆ ... (other than an event that is only a change in a specified interest rate, security price, commodity price, foreign exchange rate, index of prices or rates, a credit rating or credit index or similar variable)

=

a derivative



IASB's Framework - Focus

- ◆ General purpose financial statements to meet common needs of a wide range of users:
 - Equity investors, lenders, depositors, policyholders
 - Customers, suppliers, employees
 - Governments and government agencies
- ◆ “Tell it like it is!”



The Golden Rule

- ◆ There is a strong consensus for making transparency the ‘golden rule’ of the new international financial system.... Markets cannot work efficiently, and they will remain vulnerable to instability in the absence of adequate, reliable, and timely information from all quarters.

IMF Managing Director Michel Camdessus (IOSCO Conference, May 1999)



Elements of financial statements

◆ Balance sheet

- assets
- liabilities
- equity (= assets - liabilities)

◆ Income Statement

- income
- expense



Liability

- ◆ A **present obligation** of the enterprise arising from **past events**, the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits.



Asset

- ◆ A resource **controlled** by the enterprise as a result of **past events** and from which **future economic benefits** are expected to flow to the enterprise.



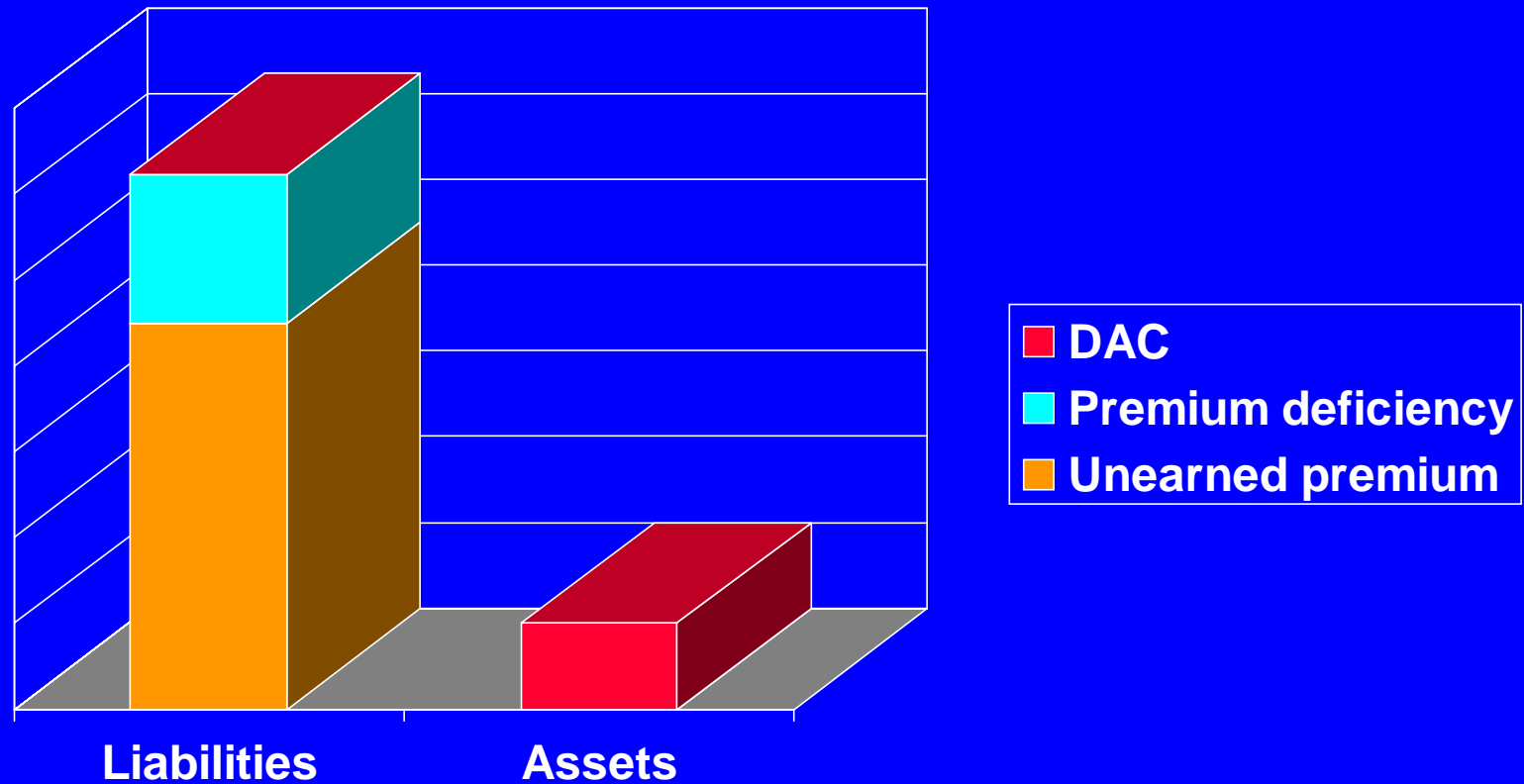
Overall approach

◆ Deferral and matching

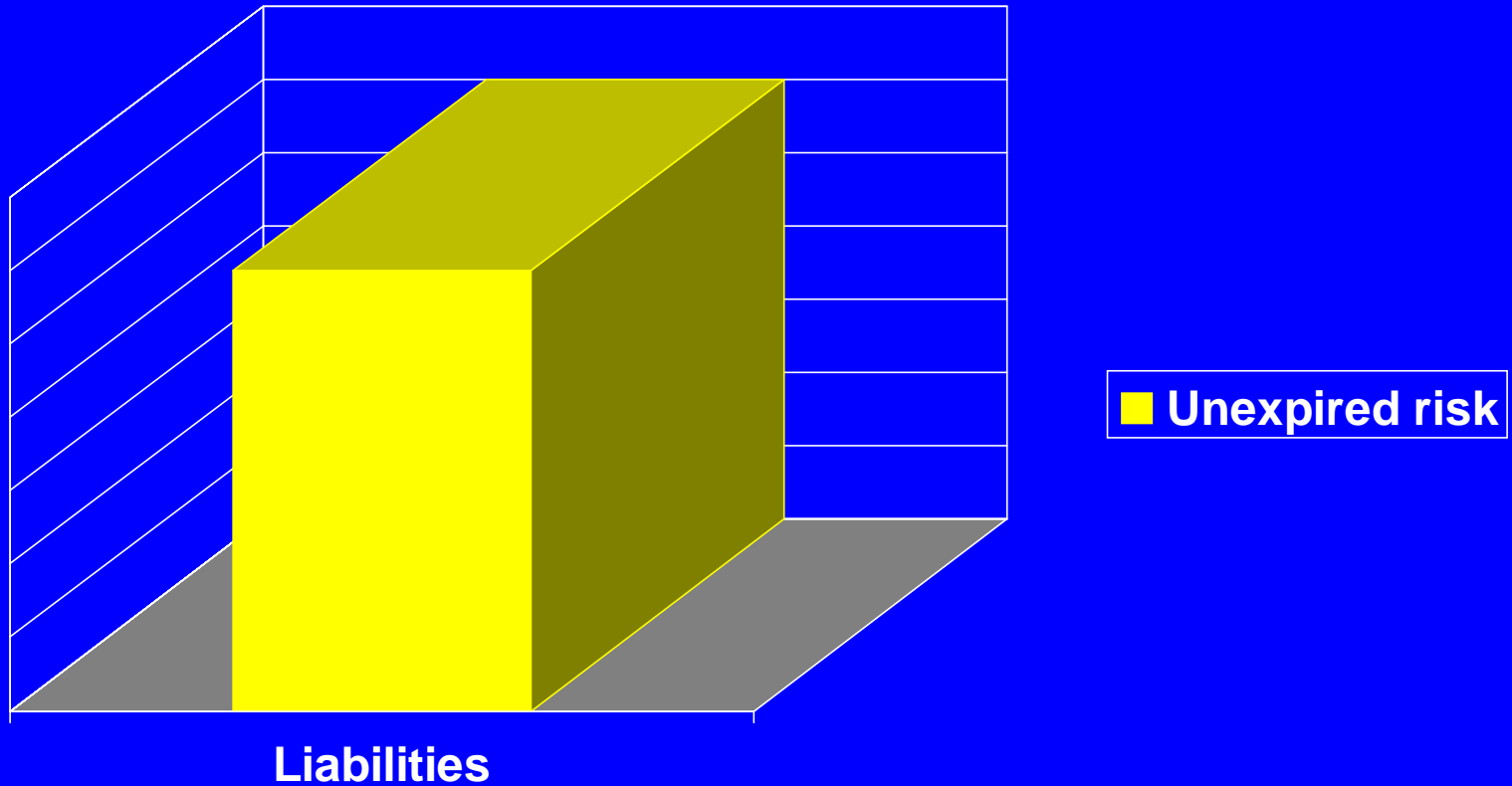
◆ Asset and liability



Deferral and matching



Asset and liability



Role of Fair Value

◆ Assumption

- a new IAS will require full fair value accounting for most financial assets / liabilities

◆ Tentative SC View

- if such a standard exists, use FV for insurance
- if no such standard, may need something else
- Issues Paper explores both



Fair Value - Definition

“The amount for which an asset could be exchanged or a liability settled between knowledgeable, willing parties in an arm's length transaction”



Asset and liability models

Fair value	No deposit floor	Investment margins?
Non fair value	Deposit floor	Do not include investment margins



Asset/Liability Interaction

- ◆ Measurement basis for insurance liabilities
 - consistent with measurement basis for assets
- ◆ Type of assets (or return on assets) should not affect actual measurement of liabilities
 - except participating and unit-linked contracts
 - fair value model: effect of future investment margins?



Unit of account

- ◆ Group of contracts that:
 - have substantially the same contractual terms
 - were priced on the basis of substantially the same assumptions
- ◆ Closed book approach
 - existing contracts (include renewals of existing contracts that commit the insurer to pricing)
 - exclude future cash flows from other possible renewals



Assumptions

- ◆ Explicit, not implicit
- ◆ Use current estimates of future cash flows
- ◆ Consider factors that are considered by the market, not factors specific to the insurer
- ◆ Reflect all future events
 - lapse
 - changes in law
- ◆ Fresh-start approach to changes



Risk and Uncertainty

- ◆ Market value margin:
 - as in price of arm's length transaction between knowledgeable, willing parties
 - disclosure?



Exit value or entry value?

- Gain (or loss) on sale?



Reinsurance

- ◆ Risk transfer
 - see definition of insurance contract
- ◆ Same accounting as direct insurance
 - deferred annual method not needed
 - gain on buying reinsurance?
- ◆ No offsetting in balance sheet



Existing Disclosure

- ◆ Financial instruments (IAS 32)
 - Terms, conditions and accounting policies
 - Interest rate risk
 - Credit risk
- ◆ Provisions (IAS 37)
 - Changes in provision
 - Uncertainties



Other Possible Disclosures

- ◆ Regulatory solvency margins
- ◆ Key performance indicators (such as sum insured in life, retention / lapse rates)
- ◆ Risk adjustments
- ◆ Sensitivity / value-at-risk



Capital adequacy?

- ◆ Accounting question:
 - How much capital **DOES** a company have?
(What are its assets and liabilities?)
- ◆ Supervisory / management question:
 - How much capital **SHOULD** a company have?
(what assets should it hold to safeguard the interests of policyholders?)



To Know More about IASC ...

- ◆ Our web site www.iasc.org.uk
 - includes project summary
- ◆ Newsletters:
 - insight (quarterly)
 - update (after each Board meeting)
 - news from the SIC (after each SIC meeting)

