

International Accounting for Insurance Contracts

General Overview

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Session 79

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Driving influences

- International Organisation of Security Commissions (IOSCO)
- International Association of Insurance Supervisors (IAIS)
- Joint Forum
- European Union
- International Federation of Accountants (IFAC)

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International Accounting Standards Board
(IASB) to develop a new International
Financial Reporting Standard (IFRS)

as a high-priority, leadership project



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Accounting concepts

- Reliability
- Recognition
- Unit of account
- Measurement

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Accounting concepts

From the IAS Framework:

An item should be recognised if:

- It is probable that any future economic benefit associated with the item will flow to or from the enterprise; and
- the item has a cost or value that can be measured with reliability.

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Accounting concepts

Actuarial and accounting concepts only converge if 'unit of account' is defined as a portfolio of similar contracts large enough for application of the law of large numbers

This is reflected in the DSoP by changing the recognition criteria.

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Draft Statement of Principles (DSoP)

- Largely published on IASB web site
- Key remaining chapters:
 - Performance linked contracts
 - Disclosure
 - Performance reporting expected by end of March

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DSoP

Definition of insurance contract: involving material insurance risk, i.e., timing, severity, or development risk that does not merely arise from a change in a price or index.

Standard applies to insurance contracts rather than to enterprises.

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DSoP

- Use of most current info rather than historical info such as pricing
- Credible data: high degree of rigor
- Actual assets that back the insurance contract are deemed irrelevant unless the benefits are directly linked with the assets.
- Credible info about the future may require the use of probability distributions rather than point estimates.

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DSoP

DSoP recommends 'entity specific' values rather than 'fair' values, but ESV definition not yet clear or accepted.

The best estimates will be estimates that are appropriate to the circumstances of a company that intends to hold the obligation rather than appropriate to a company that intends to dispose of the obligations.

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Key Insurance Problem under IFRS

- Assets mainly at FV (IAS39 being revised)
- Liabilities at ? until new insurance standard adopted
- Increased volatility and unexplainable earnings if stagger balance sheet changes

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Areas of potential conflict

Reliability concept

- At what point should adverse experience be recognised?
- Reliability in reflecting renewals; what is a valuable insurance option?
- Reliability in including future investment margins?

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Areas of potential conflict

Reliability of embedded options like:

- Guaranteed settlement options
- Guaranteed minimum interest crediting rates
- Mortality guarantees
- Maturity guarantees in index or fund linked contracts

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IASB Board developments

- Insurance accounting discussed every meeting from November to February
- Board agreement on definition and scope
- Concept of “long term contract” being examined in detail (renewal and spread issues)

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IASB field visits

- Commenced in Canada October 2001, following many countries, most recent Japan.
- Separate visits for reinsurers
- Key issues:
 - Implementation timing (costs, systems development and staff education)
 - Embedded options pricing (stochastics)
 - Financial assets
 - Presentation/disclosure and management intent

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IAA activities

- New actuarial standards setting sub-committee
- IASB insurance accounting committee preparing DSoP response
- Both standards and accounting discussion progress available from IAA web site
- Face to face meeting March 14 – 16 in Cancun

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Actuarial Standards of Practice

Work in progress:

- drafting group (8) to write papers on some 45 issues
- define what is in the DSoP
- define what is meaningful
- discuss alternative approaches
- group will consider standards for non insurance contracts issued by insurers

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Thank you very much

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