



# Insurance Accounting: Getting It Right

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Who are we?

What is the purpose of accounting?

What is at stake?

Where are we today?

What should we aim to achieve?

What are we proposing?

Why now?

→ We are a group of 20 leading European insurers from 8 countries



→ Set up in 2002 to pursue the harmonisation of financial reporting with the IASB, the Commission and other stakeholders to enhance stability, consistency and transparency for investors.

**Facilitate  
more efficient  
financial markets**

- **Giving transparent and comparable information of a company's financial position**
- **Providing for optimal understanding and guidance for shareholders, investors and other users**

## Insurance is vital for the economy...

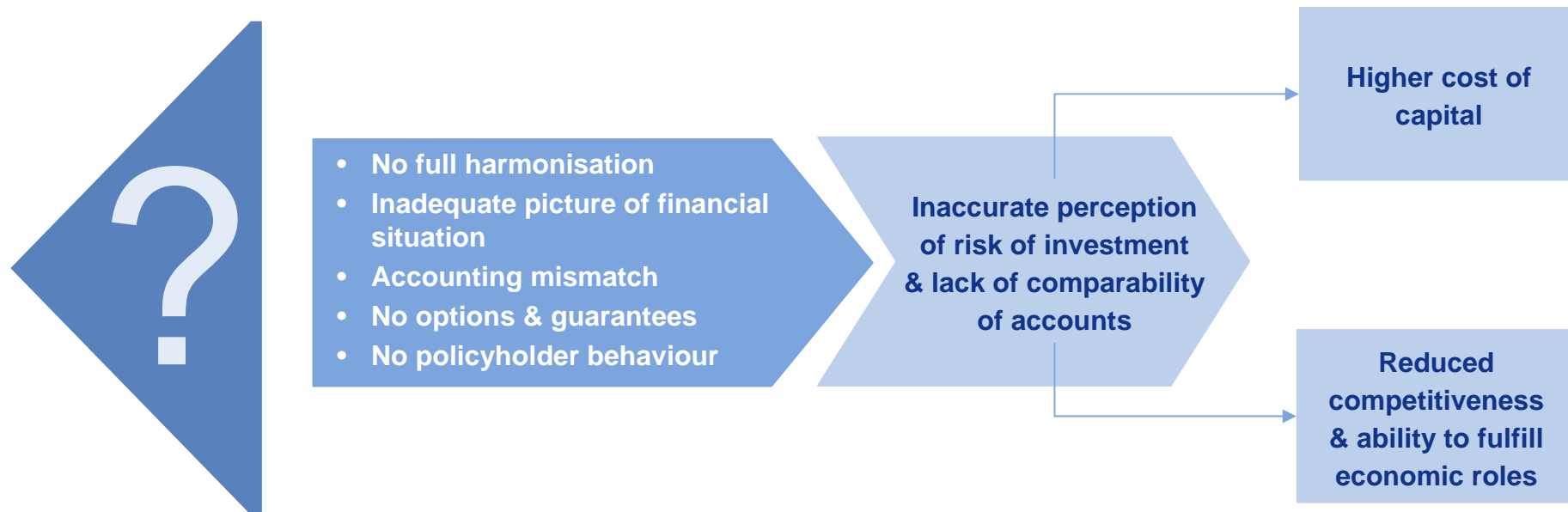
*“The trade of insurance gives great security to the fortunes of private peoples, and by dividing among a great many that loss which would ruin an individual, makes it fall light and easy upon the whole society.”*

Adam Smith

...hence the importance of a healthy insurance industry

Role of insurance	Impact on larger economy
Risk absorber	Pools risk within a large group, limiting risk for the individual Enables growth
Risk mitigator	Prevents economic loss Protects resources
Savings manager	Provides long-term savings and old age provisions Enables sustainable income in old age
Institutional investor	Significant long-term investor in public and private sectors Drives and stabilises financial markets
Major employer	1 million people directly Contributes to households income and consumption

## Current accounting framework a handicap for insurers





**International  
Accounting Standards  
Board®**

Drafts international accounting  
standards (IAS and IFRS)  
applicable in EU  
since 1. 1. 2005



Each standard needs to be  
endorsed by EU  
to become mandatory for  
+/- 7000 listed companies



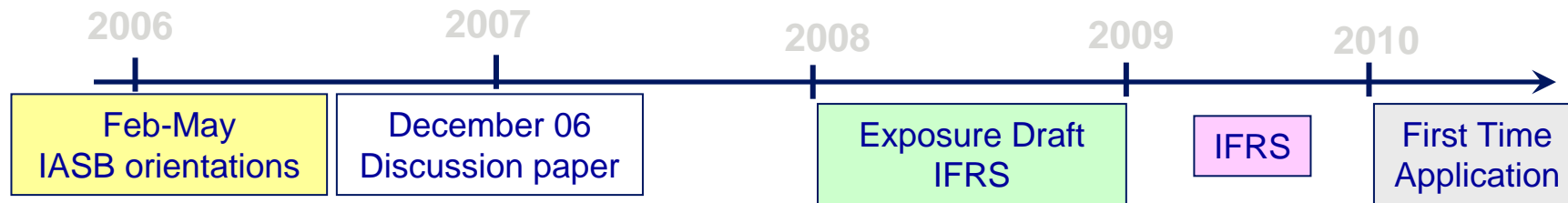
The accounting framework  
**for insurance**  
is still under development...



No final standard for insurance  
contracts (mainly liabilities)  
before 2009 or 2010



## IASB Phase II Project – Timetable

Tentative orientations

- **Prospective model** (future cash flows, discounted at market conditions, including margin for risk):  
 “Current exit value” (transfer to another insurer at market conditions: “B to B” model; possible recognition of gain at inception) rather than “Current entry value” (“B to C” model; no profit at inception)

But still hesitation on recognition of up-front profit:

“Current exit value” would include a **profit margin**

Profit at inception should be limited to actual amount of profit margin in premium in excess of profit margin charged by reference market participants if any (practically in most cases no profit at inception)

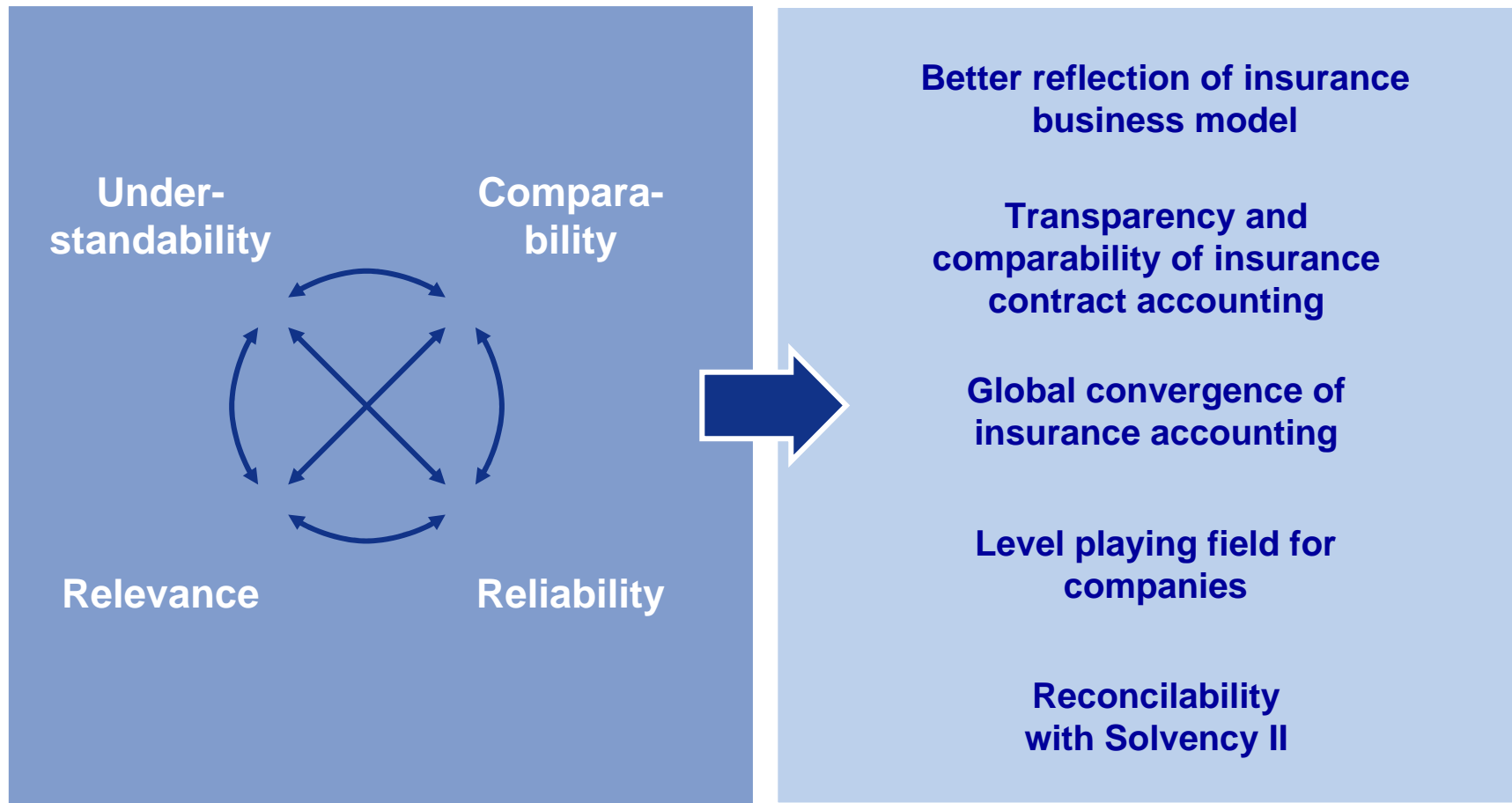
- **Participating rights:** only recognized as a liability when the insurer has an unconditional obligation which compels it to transfer economic benefits to policyholders (current or future)

- **Acquisition costs** as expense but customer relationship asset corresponding to the guaranteed assuredness possibly to be recognized (in deduction of liabilities)

- **Cost model** rejected both for insurance liabilities and for assets

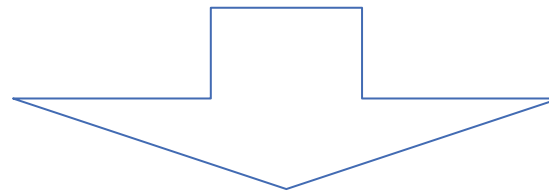
What we are seeking in our financial statements...

...and how it will benefit users and other stakeholders



July  
2005

Publication of *Principles for an IFRS Phase II Insurance Accounting Model*, a set of *high level* principles that outline the direction that the CFO Forum believes the new IFRS standard should take.



June  
2006

Publication of ***Elaborated Principles for an IFRS Phase II Insurance Accounting Model***. Since the initial publication of high level principles, the CFO Forum has worked to expand and clarify them by creating the *Elaborated Principles*. The Basis for Conclusions provide insight into the rationale for the *Elaborated Principles*.

## Collaborative and consultative process

- Reflects the insurance business model, including participating contracts
- Developed with due consideration of the IASB's goals
- Carried out rigorous development process since September 2005 involving senior staff of all member organisations and consuming in excess of 430 man days.
- Sought to give rationale to the *Elaborated Principles* by providing a Basis for Conclusions
- Detailed generic product level modeling to test impact
- Adopted by CFO Forum and supported by CEA
- Discussion with other industry groups – CRO Forum, GNAIE, LIAJ
- Ability of industry to speak with one voice having engaged in detailed and thorough debate

## Industry agreement

- Anticipated benefits of industry agreement include:
  - Increased level of acceptance
  - Increased quality of financial reporting

## A single model for life and non-life

### Reflect the insurance business model

- Profit recognised in line with release from risk

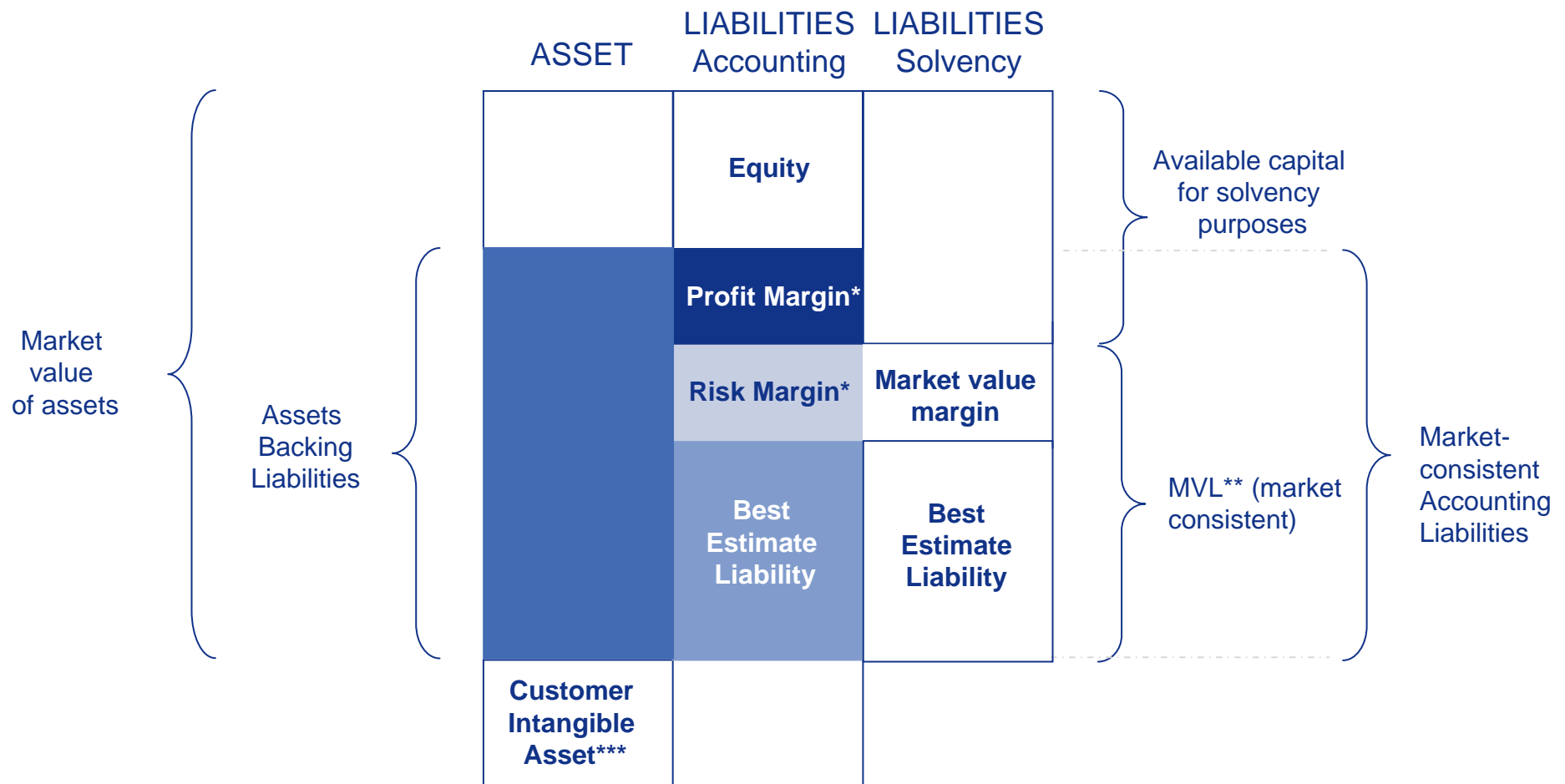
### Market consistent valuation of liabilities

- Present value of future cash flows with allowance for risk and uncertainty
- Risk free discount allowing for liquidity, with recognition of options and guarantees

### Reflect how insurance companies manage risk

- Liabilities measured on a portfolio basis reflecting policy-holder behaviour
- Assets and liabilities measured on a consistent basis

A coherent framework

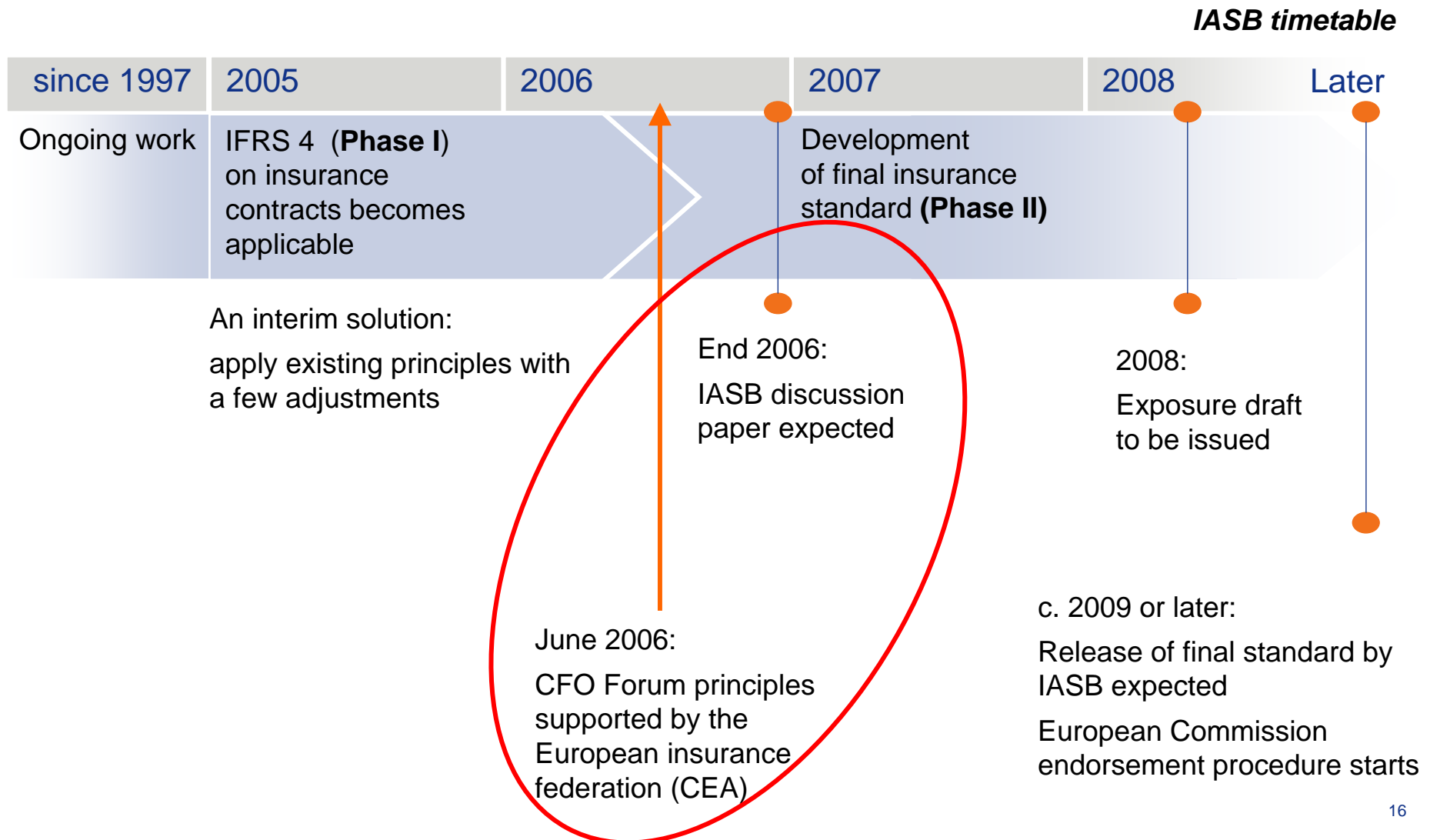


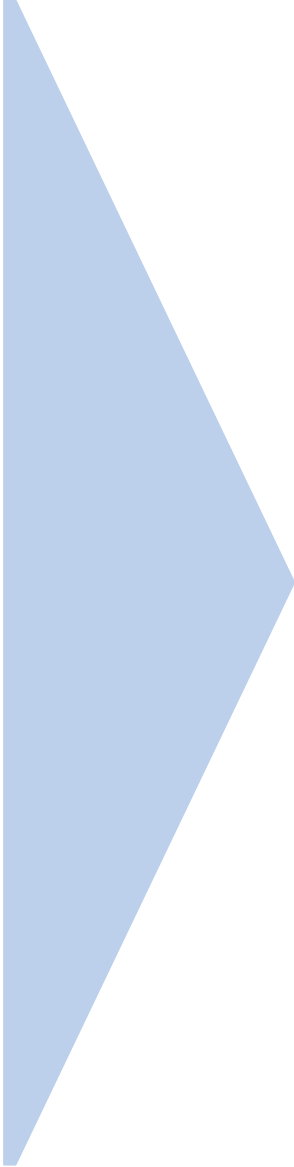
\* CFO Forum Total margin including allowance for risk and future profits

\*\* CRO Forum Market Value of Liabilities being for non-hedgeable risks the best estimate plus the market value margin (with a cost of capital as a proxy)

\*\*\* CFO Forum CIA = Customer Intangible asset (for accounting purpose, shown as an asset together with gross liabilities)

## Our work is now at a very important stage





Standard-setting should be anchored in business reality in the interest of investors and other users.

We support change, but change needs to truly enhance transparency and comparability.

Our proposals meet the needs of users and are endorsed by the entire European insurance sector.

We look forward to discussing our proposals with you.