



International Association for the  
Study of Insurance Economics

# Études et Dossiers

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# Financial Reporting and Disclosure by Insurance Companies – International Survey of Users' Needs

Gerry Dickinson

Research by The Geneva Association  
(see [www.genevaassociation.org](http://www.genevaassociation.org))

- **'The Search for an International Accounting Standard for Insurance' by Gerry Dickinson, 2003**
- **'Impact of a Fair Value Financial Reporting System on Insurance Companies: A Survey' by Gerry Dickinson and Patrick Liedtke, 2004**
- **'Financial Reporting and Disclosure by Insurance Companies – International Survey of Users' Needs', 2006**

Primary goal of financial reporting is pragmatic provision of information to help users, particularly investors/creditors, in making their decisions

- **There is no agreement, nor likely to be, on what is a correct theoretical basis for financial reporting and information contained in financial statements**
  - ‘Accountants have adopted a decision-usefulness approach to financial reporting as a reaction to the impossibility of preparing theoretically correct financial statements’,  
W.R Scott (University of Waterloo, Canada) ‘Financial Accounting Theory’, 2003
- **The current conceptual frameworks of the IASB, and the FASB and other national standard setters, state that the primary aim of financial reporting is their value to users in their decision-making, with a emphasis on investors and creditors and those that advise them**
  - ‘The FASB’s goal in setting standards is to enhance the usefulness to investors and creditors of the information entities report in financial statements and other financial reporting’, L. Todd Johnson ‘Relevance and Reliability’, FASB Report, Feb 28, 2005

2

The challenge is to assess ‘What investor, analysts and other users want’

- **It is difficult for accounting standards setters to assess users needs systematically. Instead standards have been predicated on the following characteristics of information.**
  - Relevance, reliability, comparability and understandability, within an overarching requirement of a high level of transparency
  - In March 2006, FASB and IASB have issued a short on-line questionnaire ( 5 questions) to users of financial statements to see how more disclosure on the fair values on financial instruments would be more useful to them.
- **Reliability and comparability can be assessed *a priori*. But relevance depends on what users consider as beneficial and on what markets (esp. capital markets) judge as significant in forming, and revising, expectations on corporate performance.**
  - What users consider as beneficial can be assessed by seeking their views (viz. extensive surveys and interviews) and by understanding their decision-making processes
  - What markets consider as useful is harder to assess, since it can only be inferred from empirical evidence on how market participants react to new accounting information. The impact of fair value accounting cannot tested as fair values are only partially used in practice.

3

User needs survey to assist development of new IFRS's

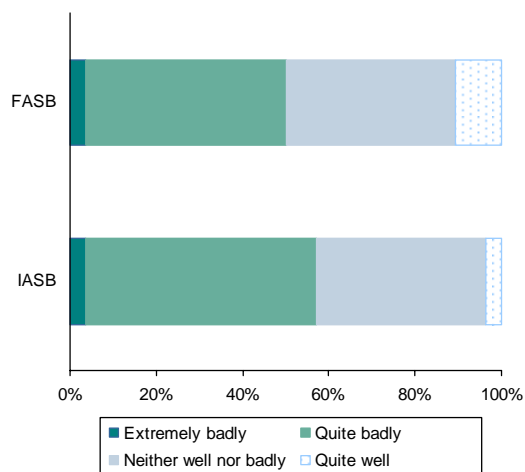
**Objectives**

- Identify the key information from the financial reporting of insurance companies to assist users in their decision-making
- Assess user views on the current IFRS regime
- Identify the information priorities of users to ensure that future IFRS's can be designed to best meet their needs.

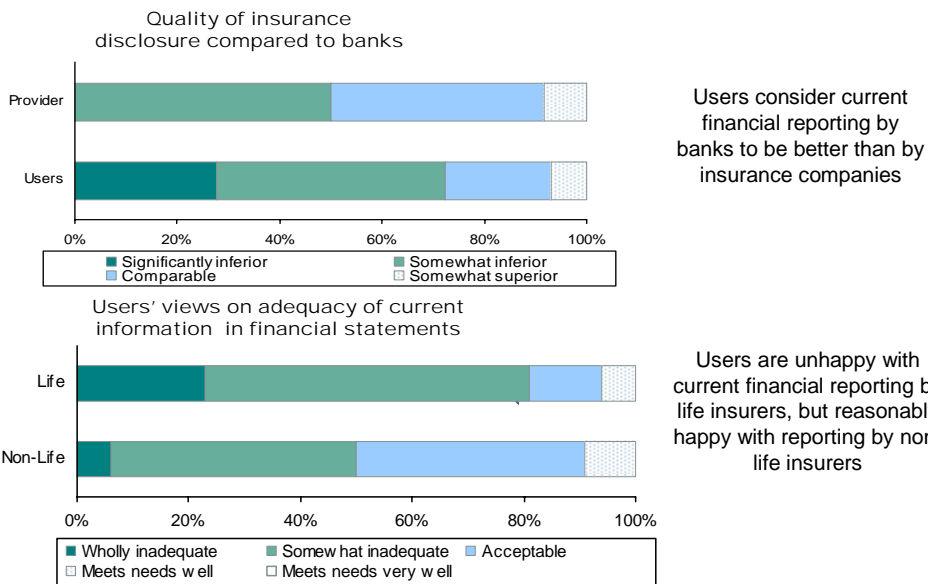
**Process**

- A survey has been mailed to over 220 recipients covering various types of users: investors, financial analysts, hedge funds and rating agencies. (Insurance supervisory authorities to be added)
- Response rate (so far) : 22%

How effective have the IASB and FASB been in incorporating user views and needs when developing financial reporting standards

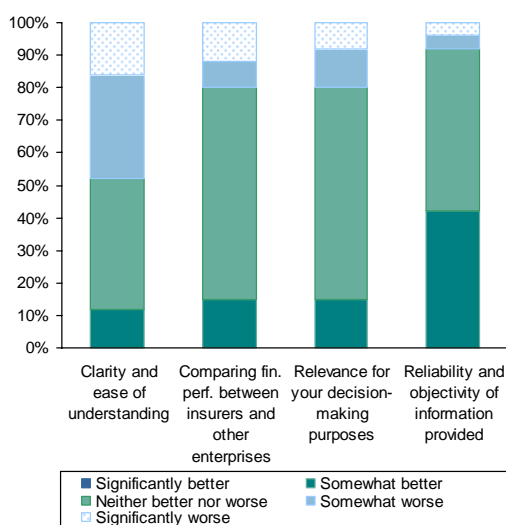


Current situation – major difference in views between insurers and users on adequacy and quality of financial reporting and disclosure

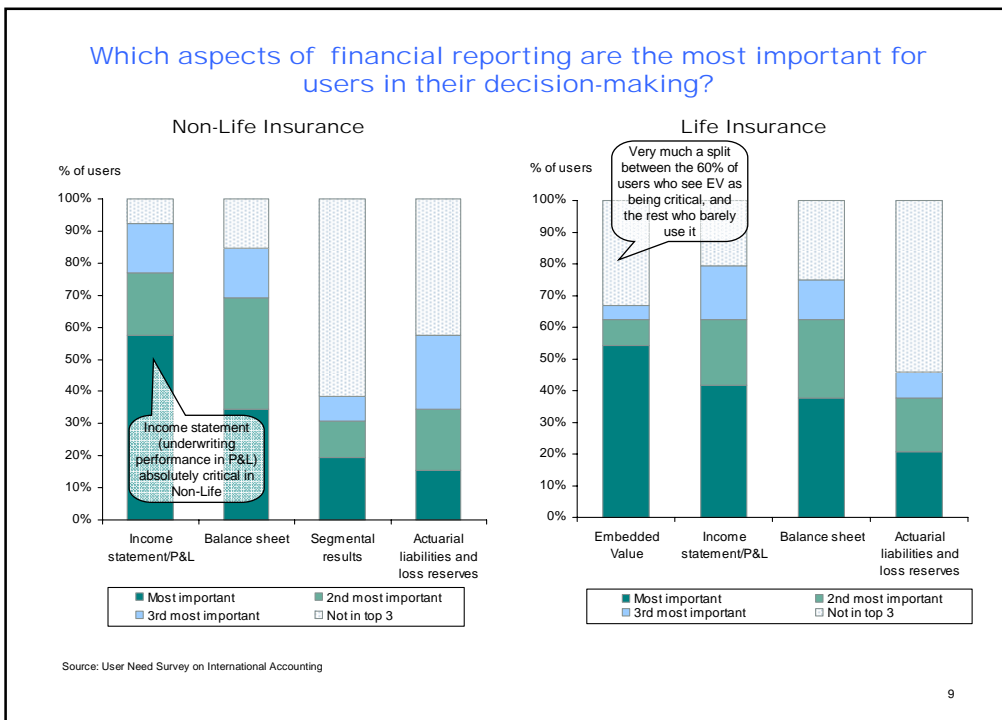
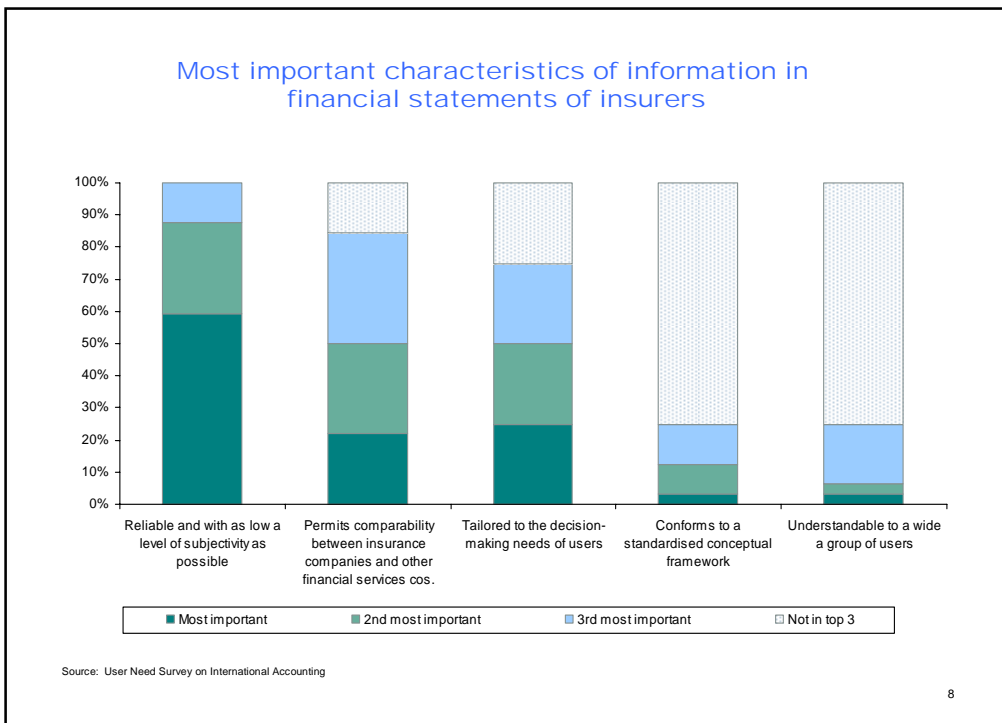


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Improvement in relative usefulness of financial statements of insurance companies since introduction of IFRS4 and IAS39

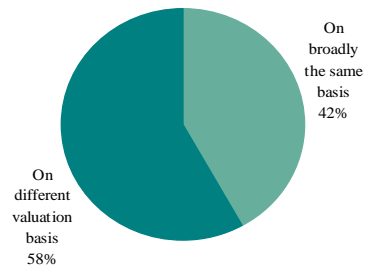


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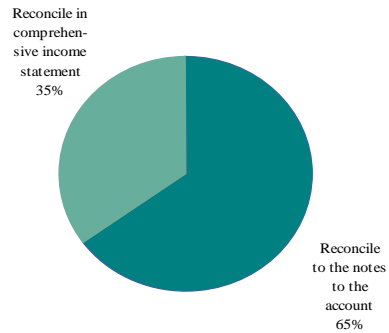


Over a majority of the users would prefer different approaches in the measurement of earnings and equity capital measurement

Measurement of earnings and equity capital should be on same valuation basis or can be on different basis



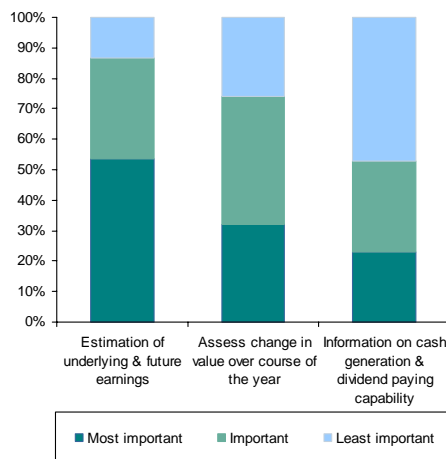
... with reconciliation in the notes to the account or in a comprehensive income statement?



Source: User Need Survey on International Accounting

10

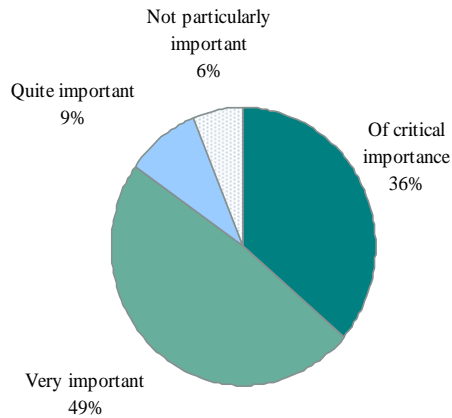
Most important use of insurers' income statements



11

Market value/fair value disclosures important, but users prefer to see any impact of changes in a Comprehensive Income Statement than directly in Income Statement or in Equity.

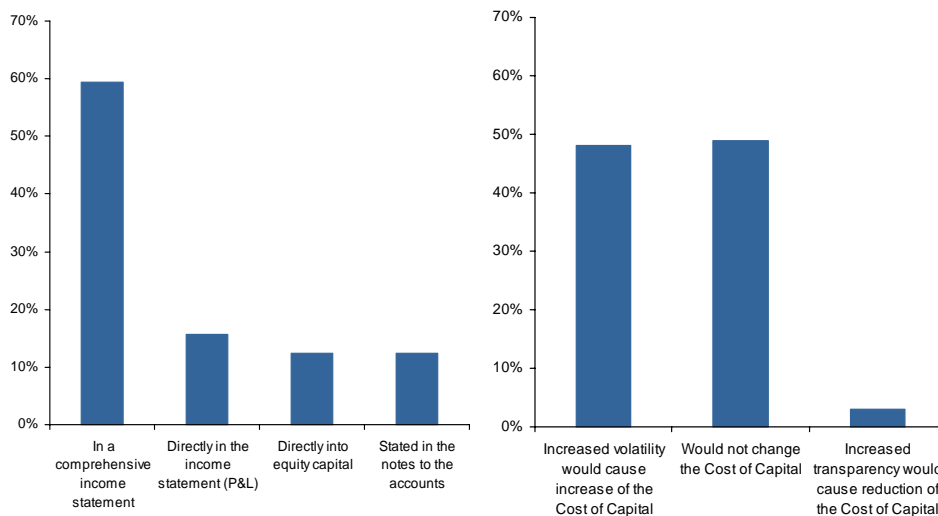
Importance of market value disclosure of all financial assets/liabilities, when they can be measured reliably.



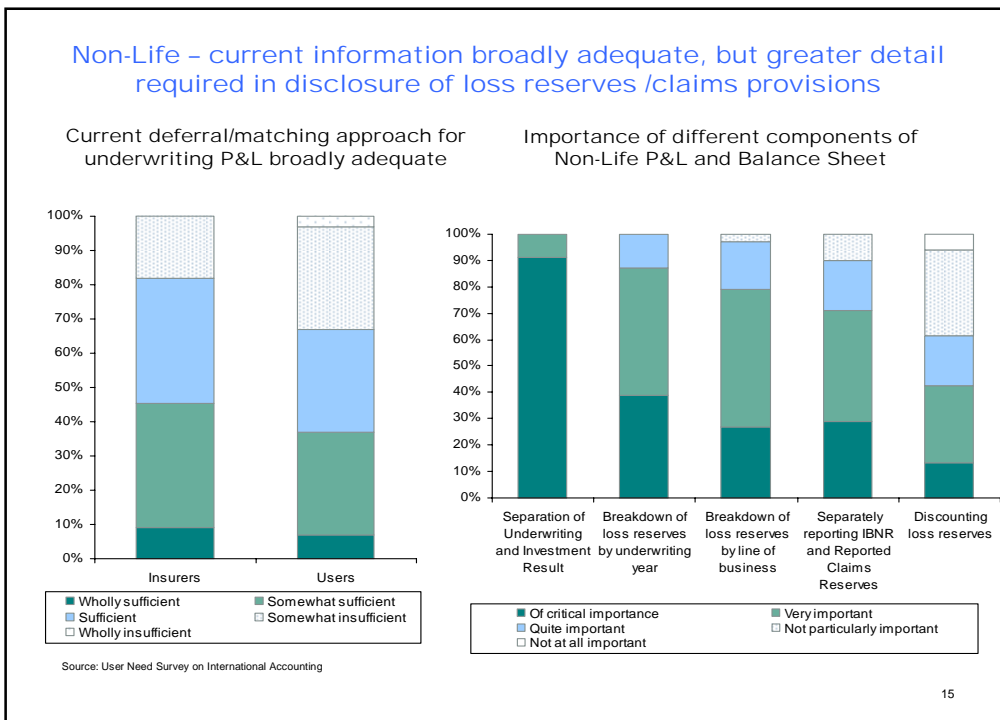
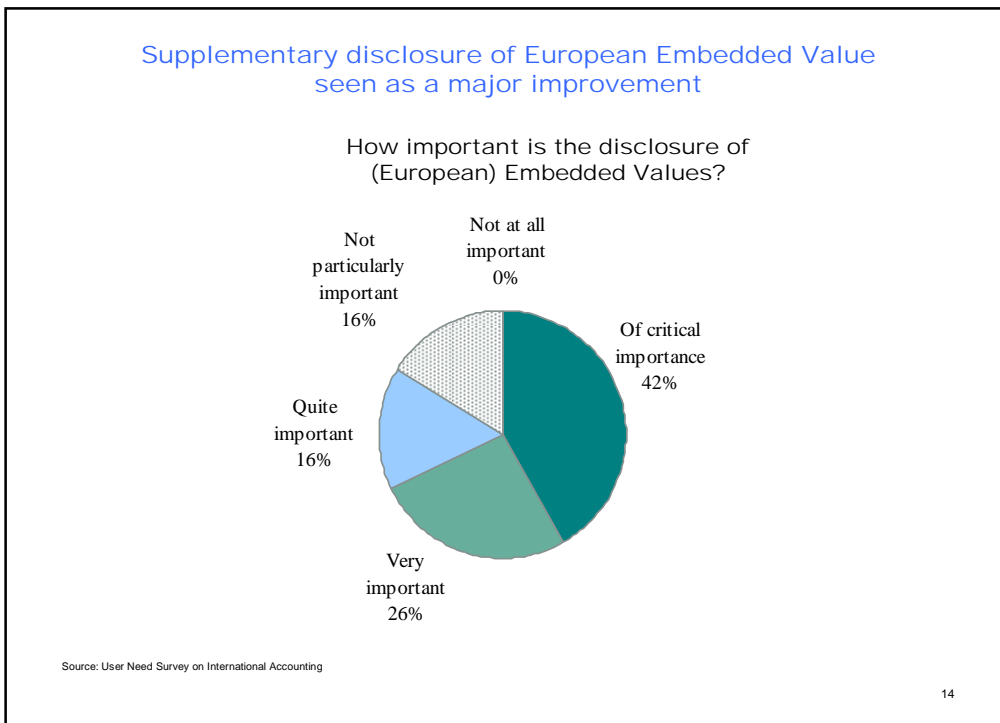
Source: User Need Survey on International Accounting

12

Where should changes in market value of unrealised gains/losses be reported? Expected effect on cost of capital of increase in volatility of reported earnings

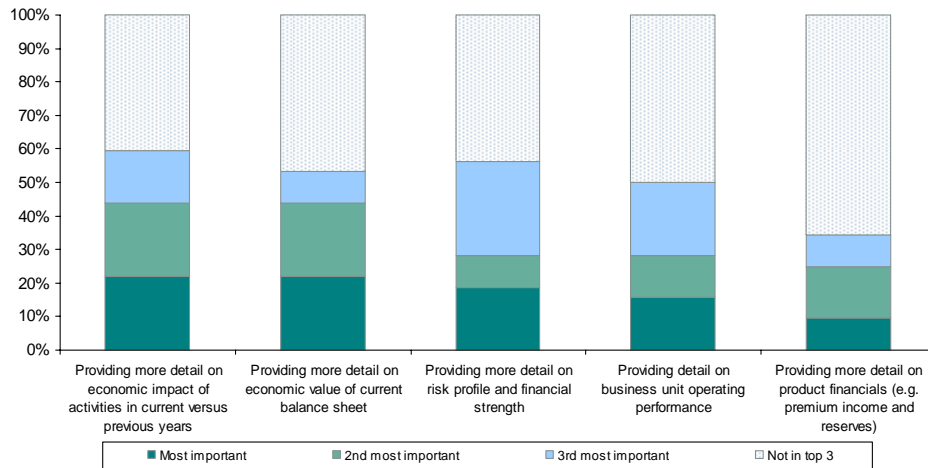


13



Life – Users want greater transparency. . . both of current balance sheet, and value of new business

Where should current information in the financial statements of life insurers be improved?

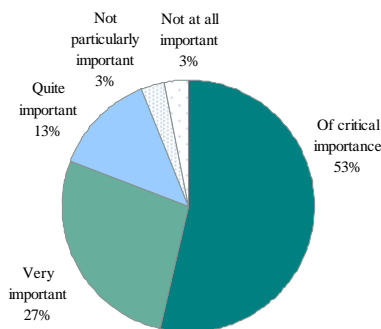


Source: User Need Survey on International Accounting

16

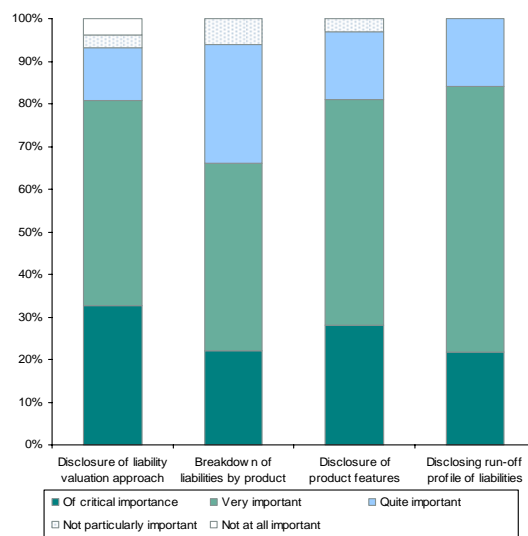
Life (cont'd) – Enhanced disclosure of new business versus in-force performance and asset-liability profile particularly important

Differentiation between new and in-force business

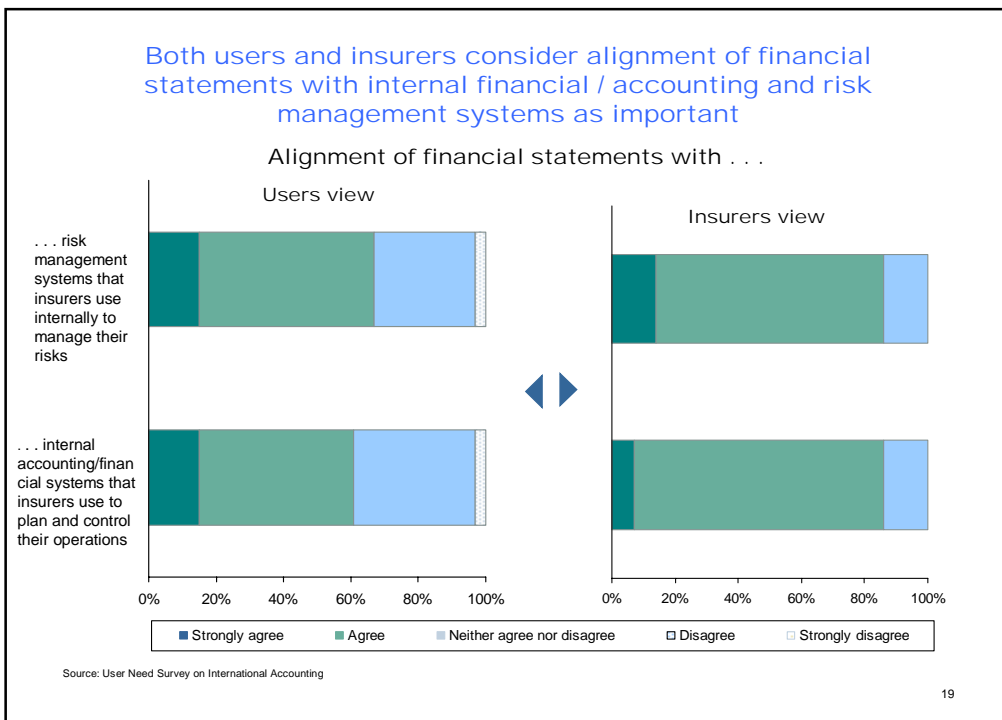
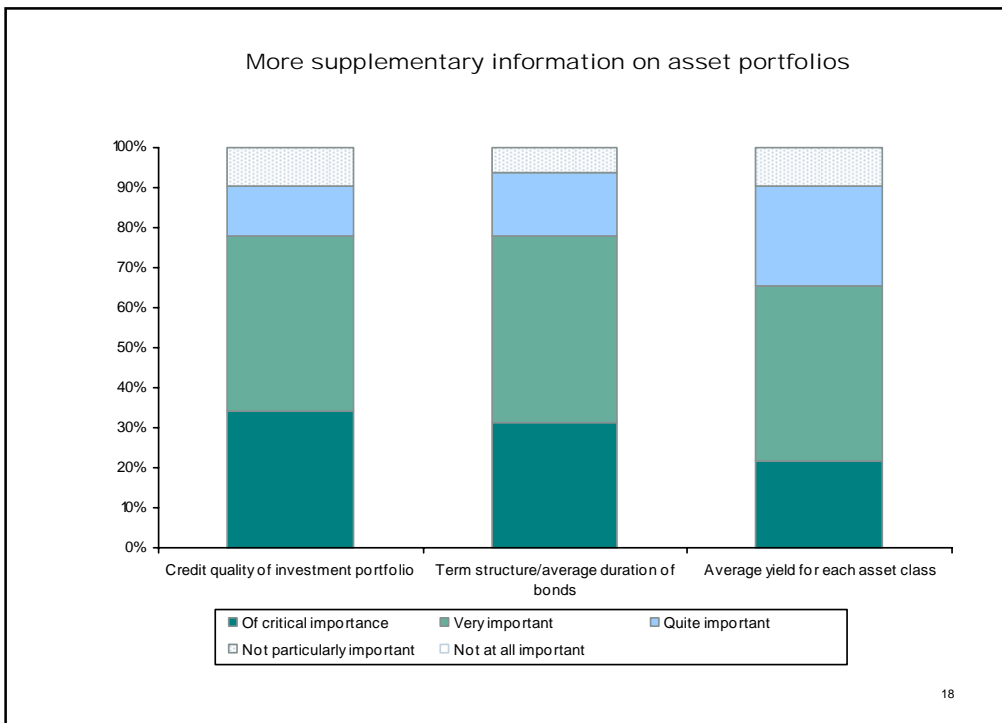


Source: User Need Survey on International Accounting

Disclosure of life technical provisions

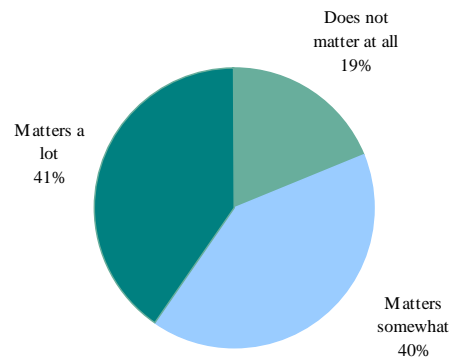


17



### Impact of a new financial reporting system on products and on business models and policies would matter

How much would it matter if a new financial reporting system were to significantly change the products and business models and policies of insurers ?



Source: User Need Survey on International Accounting

20

### Conclusions

- Users believe IASB and FASB have not done a good job so far in incorporating their decision-making needs into their accounting standard setting processes.
- Users (European) find the new European Embedded Value supplementary reporting a major improvement. US and Japanese users still do not incorporate embedded values into their key analysis.
- IFRS 4 and IAS39, with more detailed disclosures in the notes, have improved comparability, relevance and objectivity. But financial reporting based on IFRS regime lack clarity and ease of understanding. This is not a problem for leading analysts and large investors but it is a problem for smaller investors without access to internal or external expertise to interpret the more complex financial statements and disclosures.

21

- There is still a significant mismatch between actual and preferred quality of financial reporting.
  - This perception of the quality of financial information differs significantly between the providers (insurers) and the users (investors, analysts, rating agencies)
  - More detailed disclosure of accounting data and underlying assumptions are needed.
- Investors, analysts and rating agencies in general use their own models and measurement metrics to assess and forecast financial performance
  - It is the information in the financial reporting system that matters more than the formal structure of financial statements. Professional users have access to other information in addition to the information in financial statements and disclosures.
  - Users are mainly concerned with forecasting the key drivers of future financial performance, especially components of the core insurance businesses.

22

#### Users want improvement in following areas

- Reliability of information in financial statements, with a low level of subjectivity by preparers, to assist in forecasting their future performance and which allows greater comparability between insurers and assess changes over time.
- More detailed relevant information. Users in the United States are much less dissatisfied as the SEC, market practice and statutory reporting ensures a good deal of supplementary disclosure.
- Financial statements that better reflect the underlying economics of the insurance business, and disclosure of the market value of assets and fair value of liabilities if they can be measured reliably.
- However, users have a preference for disclosure of any changes in market/ 'reliable' fair values of assets and liabilities into a Comprehensive Income Statement not directly in an Income Statement (P&L) or directly in Equity.
- Greater alignment between external financial statements and internal accounting / financial planning / risk management (ALM) systems within insurance companies.

23

### Summary of main views on financial reporting for non-life insurance

- Current system of measuring underwriting profit (loss) based on deferral and matching is considered broadly acceptable, providing reserving methods are sound and realistic. The combined ratio is widely used as a metric to measure and compare underwriting performance between companies, classes of business and to analyse trends over time
- Greater disclosure of loss reserves and valuation methods used, although discounting itself is not a key concern. If run-offs patterns of claims are disclosed, they can and prefer to do their own discounting.
- Clear separation of underwriting performance from investment performance. It is important to have a clear picture of the underwriting profitability and its main components (premiums, claims, expenses, reinsurance arrangements etc) but with a more detailed breakdown of accounting data by types of insurance business and by geographical region.

24

### Summary of main views on financial reporting for life insurance

- Less satisfaction with life than non-life insurance reporting, especially within Europe.
- Users want a clear separation of new business from the in-force business and more consistent measurement of assets and liabilities on a market-related basis. ALM matters more in life than in non-life.
- European users want embedded values as supplementary information, especially if comparable between insurers as under EEV. US and Japanese users still have little interest in embedded values.
- More detailed disclosure of asset-liability profiles and structure of assets and liabilities.

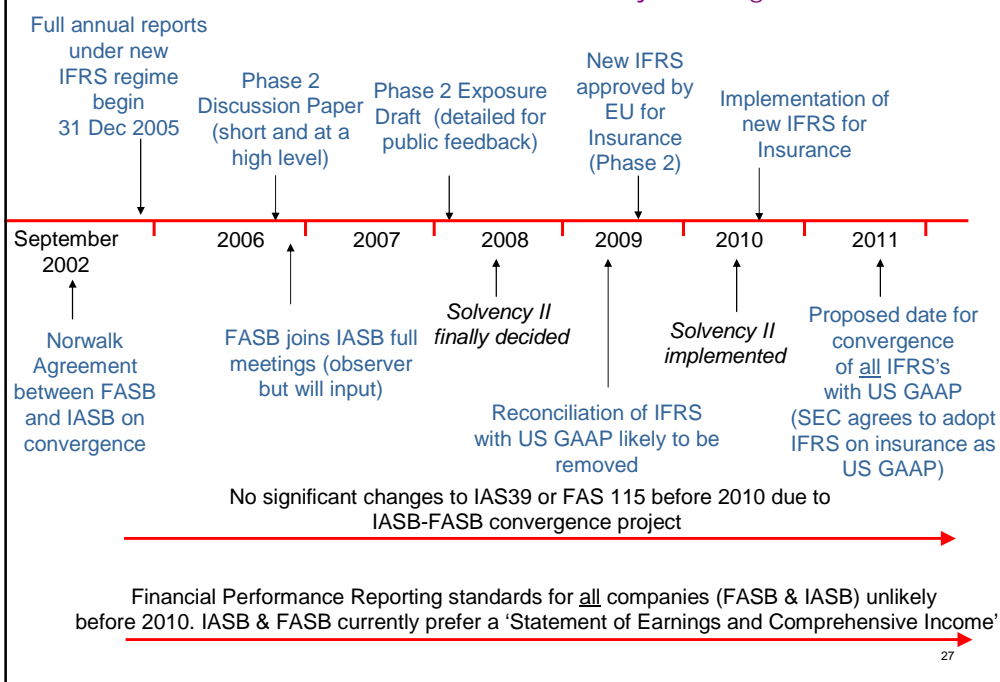
25

Relevance of Survey to IASB and FASB

- Phase 2 of Insurance Contract Project (IFRS and eventually part of US GAAP and other national GAAP's, if the IASB and FASB convergence project succeeds)
- Financial Performance: Reporting for Business Enterprises (FASB and IASB). FASB and IASB have preference for a single income statement with subsections: 'Statement of Earnings and Comprehensive Income'. (This would be for all industries)
- Possible future changes to IAS39 and FAS 115 from on-going joint projects of FASB and IASB on 'Financial Instruments' and 'Fair Value Measurement'
- Financial Instruments: Liabilities and Equity ( FASB and IASB)

26

Probable Time Scale for the Major Changes Ahead



27