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What a Year!

by Henry W. Siegel

It's customary in columns such as this to summarize what has happened during the year, to contrast where we are with where we started and to offer some predictions for the future. Unfortunately, events have overwhelmed my ability to capture them. The collapse of Lehman Brothers, AIG and so many other financial firms, the possible, still unresolved potential bankruptcy of the Big 3 car companies and, the cherry on top, the fraud of Bernie Madoff, show clearly that nothing is impossible, nothing can never happen and nothing is beyond the realm of the conceivable. It's like the novelists have taken over the world for a year. How can anyone summarize such developments in a few paragraphs?

In fact, I look forward to reading several books on these topics.

From the perspective of insurance accounting, however, the year has been lots of talk and very little progress. The International Accounting Standards Board (IASB) and its staff have been struggling with how to respond to comments on their Discussion Paper that almost unanimously disagreed with the tentative positions they'd taken.

At the same time, the Board published discussion papers on Financial Statement Presentation and Revenue Recognition that could greatly influence the insurance standard. On the U.S. front, the SEC published a proposal for how the United States would move to have International Financial Reporting Standards (IFRS) replace US GAAP for general purpose accounting.

Most surprising to some, the NAIC has also started to look at international issues, making it a real possibility that IFRS might one day become the standard for U.S. Statutory accounting as well as for general purpose accounting.

Overall, then, this was a relatively quiet year and a fairly quiet quarter on the insurance front.

OCTOBER

The IASB's discussion of a measurement attribute for insurance was anticlimactic, like almost everything this quarter that wasn't directly connected to the economic crisis.

Staff gave the Board five alternatives. In order, they were:

1) Current Exit Value as described in the Discussion Paper.
2) Market Value as described in the CRO Forum's paper on the subject.
3) The CFO Forum's proposal which took the CRO Forum's proposal and added a liability to prevent gains at issue.
4) The Group of North American Insurance Enterprises proposal which calibrates margins to premiums to eliminate any gain at issue and, in a surprise return,
5) Unearned Premium Reserve (UPR).

In their paper, options 2-4 were described as fulfillment value proposals. Details of each proposal can be found in the Observer's Papers or on the Web site of the cited organizations.

The major difference between the proposals is in how they handle gains at issue. Options 1 and 2 would allow gains or losses at issue, Options 3-5 would not. Of course, the UPR deals only with pre-claims liabilities and board members agreed that it applied well to short-term policies and matched well with their revenue recognition positions.

The Board's discussion of the alternatives was quite expansive; Board members spoke in favor of each of the alternatives and no vote was taken.

The same week, the IASB also published a long discussion paper on Financial Statement Presentation. Comments are due in April and it is sure to receive a lot of them. Among other changes, the proposal in the paper would eliminate the traditional Balance Sheet with assets and liabilities on opposite pages and would create a consolidated income statement that combines the traditional income statement with all the items in Other Consolidated Income. At first glance, it does not appear that there are any major problems with the proposal from an actuarial perspective, but it's clear that insurance contracts will require special disclosure information of their own.

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NOVEMBER

The highlights of November were the International Actuarial Association (IAA) meeting in Cyprus the first week of the month and the Insurance Working Group (IWG) meeting the following week.

The IAA meeting was notable in that the Accounting Committee's paper on Current Estimates and Risk Margins was discussed and the task force working on it announced that a final version would be out before the end of the year. It was emphasized that this paper was a research paper and not a recommendation of the IAA. This is necessary since it's unlikely that the IAA would be able to reach a consensus on how to calculate risk margins until the IASB decides what its measurement attribute would be.

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The Accounting Committee is preparing to respond to the IASB/FASB papers on Financial Statement Presentation and Revenue Recognition.

Like the IASB meeting in October, the Insurance Working Group meeting reached no consensus. This is hardly surprising since representatives of each of the three groups proposing fulfillment value approaches was well represented at the table. Furthermore, based on comments by the board members present it appeared even clearer that the IASB itself has not reached a consensus.

Other topics discussed at the meeting included what discount rate to use for liabilities and whether movements in liabilities due to movements in interest rates should be put below the line, the same way that unrealized gains on assets are. No consensus was reached on these proposals either.

As a final touch to the month, "any day now" finally arrived and the SEC published their promised roadmap for conversion to IASB. While many feel that this conversion to a single global accounting standard is a welcome idea, there are still others who doubt that a principle-based system will work well in the litigious system present in the United States. Comments are due on this release in February and it will be the task of the new SEC head (Mary Schapiro is the nominee) to deal with the reaction, whatever it is.

DECEMBER

December was the cherry on top of one of the most amazing years in modern financial history. The Madoff fraud was a calamity that affected rich and poor alike. At this writing its extent is still being determined.

For the insurance contract project, the month yielded little new. The NAIC's International Solvency and Accounting Working Group published a more detailed plan for approaching international solvency and accounting, but it was notably long on research and omitted any target dates. There was a Geneva Association meeting on the subject of international accounting and solvency that again offered little that was new.

The IASB's revenue recognition project finally produced a discussion paper and that is possibly the most important development of the entire quarter. How it will affect the insurance project remains to be seen but it could determine what measurement attribute is ultimately adopted.

WAIT 'TIL NEXT YEAR!

Next year should be much more interesting. Not only will comments be received on the three major discussion papers published late in 2008 (the SEC Roadmap, Presentation and Revenue Recognition), but the Board will make key decisions on the insurance contracts project during the first half of the year. By the end of the year, an Exposure Draft on Insurance Contracts should be out.

Of course, all of this will be taking place in the light of a new U.S. administration and how it deals with the economic turmoil it faces.

Remember: Insurance Accounting is too important to be left to the accountants. ■