



SOCIETY OF ACTUARIES

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# Embedded Value Reporting Redux

Stop us if you've heard this one—Embedded value reporting is coming to North America. This has been heard in various forms since the late '90s. But this time it's true. Embedded value (EV) reporting is growing in importance in North America for several reasons. Most European insurance groups (and, by extension, their North American subsidiaries) are reporting embedded value results publicly. In Canada, two of the "Big Three" regularly disclose embedded values as part of their external reporting. The concept behind embedded value is similar in nature to the principles-based approaches being developed by the American Academy of Actuaries, and investment analysts and rating agencies are increasingly turning to economic measures of value other than traditional statutory or GAAP reporting.

One major criticism of embedded values has always been the lack of authoritative guidance. Because EV reporting lies outside the purview of statutory and GAAP accounting, North American standard setters have steered clear of addressing EV (notwithstanding a paper published by the Canadian Institute of Actuaries in 2000). However, with EV gaining popularity outside North America, in 2004 a group comprised of the CFOs of the major European life insurers published a set of principles for reporting embedded values. These principles, and subsequent releases, have begun to form a set of codified guidance for EV reporting that has, in part, filled that void for North American insurers.

With that in mind, the Academy's Life Financial Reporting Committee decided to further enhance the guidance available to actuaries performing EV work. The Committee is currently completing a Practice Note for North American actuaries on the reporting of embedded values. This work comes not a moment too soon. The SOA Embedded Value Webcast was attended by at least 600 people, indicating that interest in EV reporting is on the upswing, with more than half of registrants stating they were currently calculating EV in some form.

The Practice Note focuses on traditional and European Embedded Values, while leaving the thornier issues relating to Market-Consistent Embedded Values for a future Note. Topics covered include:

- Introduction to embedded values
- Mechanics of embedded values
- Non-economic assumptions
- Economic assumptions
- Analysis of movement
- Treatment of options and guarantees
- Disclosure of embedded values

As is characteristic of Academy Practice Notes, the focus is on the current state of practice in North America, although the Committee does attempt to provide some of the theoretical basis underlying certain issues. The target date for the release of the exposure draft is December 2007.

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- Errol Cramer
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