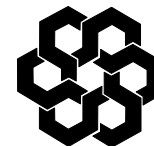


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**International  
Accounting Standards  
Board**

This document is provided as a convenience to observers at Insurance Working Group meetings, to assist them in following the discussion. It does not represent an official position of the IASB. Board positions are set out in Standards.

#### **INFORMATION FOR OBSERVERS**

**IASB Meeting:  
Paper:**

**Insurance Working Group, April 2008  
User Needs (Agenda paper 4)**

**IASB**  
**Insurance Working Group Meeting**

April 2008

Maurizio Lualdi

# The right information (quantity and quality)



*Teatro La Fenice (Venezia)*

- How far should we go in making financial information dependent on the “inner works” of the industry?
- Building “self sufficient” information levels that help generalists understanding the business.
- Manage the business / information, to make it more predictable and viable as an investment.



# Common Questions

HOW DO YOU  
MAKE MONEY?

CAN I FORECAST  
THIS BUSINESS?

SHOW ME  
THE MONEY!



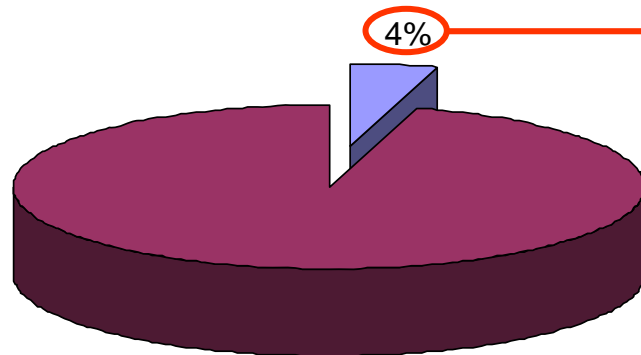
ARE YOU IN CONTROL  
OF YOUR BUSINESS?

WHAT ARE  
THE RISKS?

CAN I COMPARE YOU  
WITH OTHER SECTORS?

# Is the sector important enough to be a “special case”?

The Insurance Sector versus the Global Market



■ Insurance Sector  
■ Rest of the Market



**Stokastiko**

The insurance sector globally represents 4% of total market capitalisation.

Can you live with 96% of any universe?



The answer is probably yes, standing out from the crowd is not always a positive.

# What would I like to see...

- I would like to see how insurance companies make money and when the money gets to shareholders.
- I would like to be able to compare insurance to other sectors.
- I would like to be able to forecast, not guess.
- I would like to see a reporting framework that (allow me the use of the word) “mimics” the business dynamics.

# Form and Content

- What to publish?
  - Life insurers: margin analysis and asset development.
  - P&C: development accounts by generation by business line.
- In what form?
  - Is mark to market across the board a sensible thing?
  - Bond based business ALM matched... why mark to market? – Noise for free?
  - Equity based businesses and investments – yes mark to market.
  - Avoid management misbehaviour driven by accounting.

# Modular Reporting



Where I would like to be.....where I am...

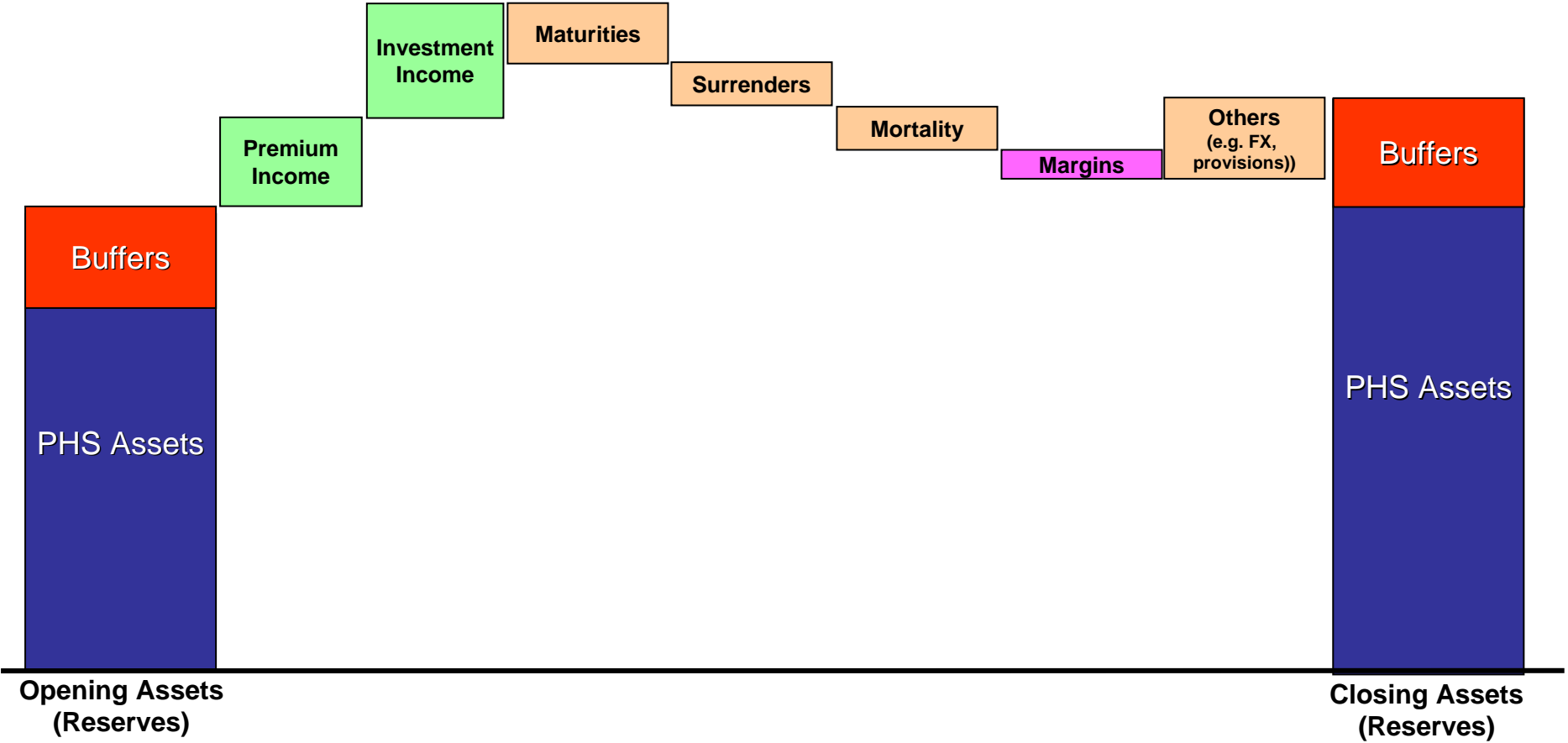
My vision...

Build a reporting framework that is modular. Degrees of complexity are added but the first level of disclosure allows for basic understanding of the business, from Margin Analysis and Asset Development to Value at Risk. If you want to be a PhD in insurance be it, but don't have this as a requirement to be able to invest in the sector.

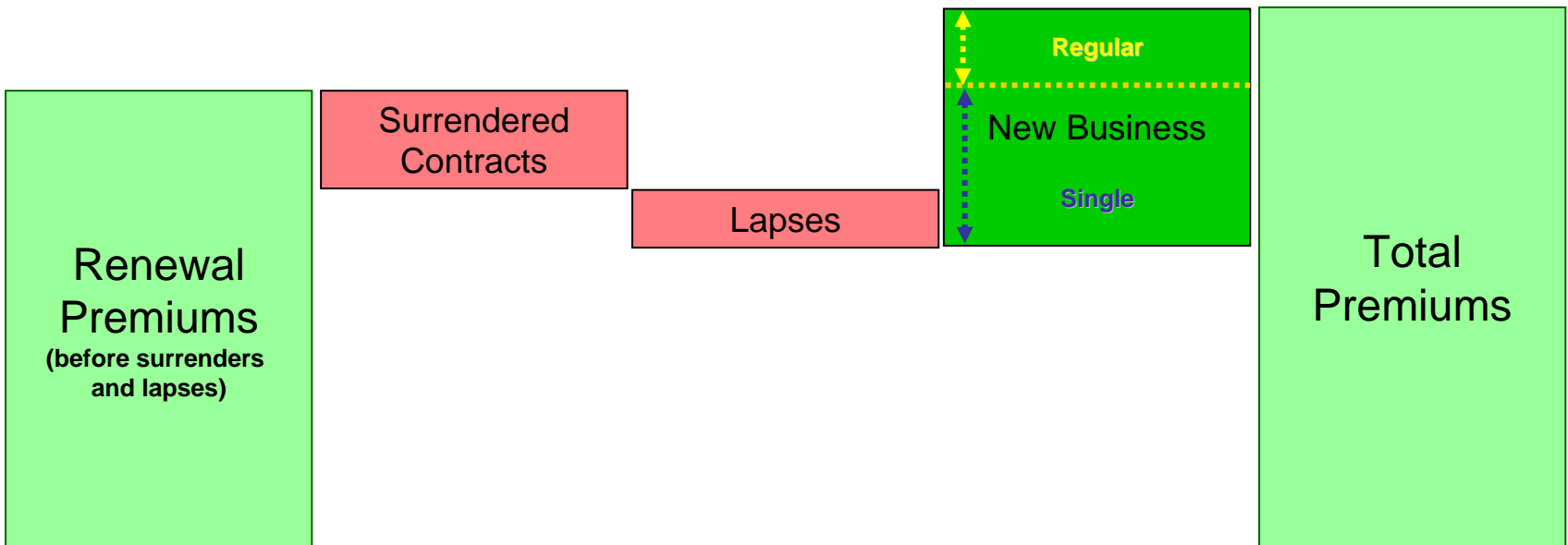
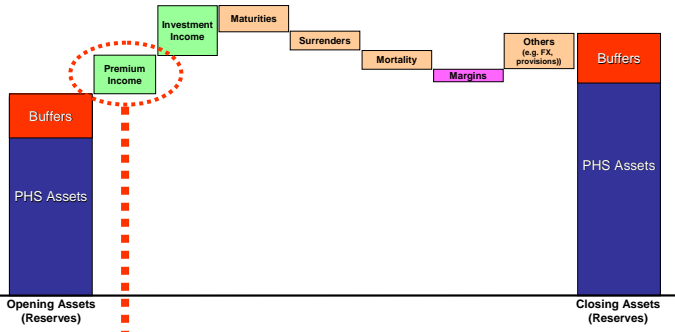


# Life

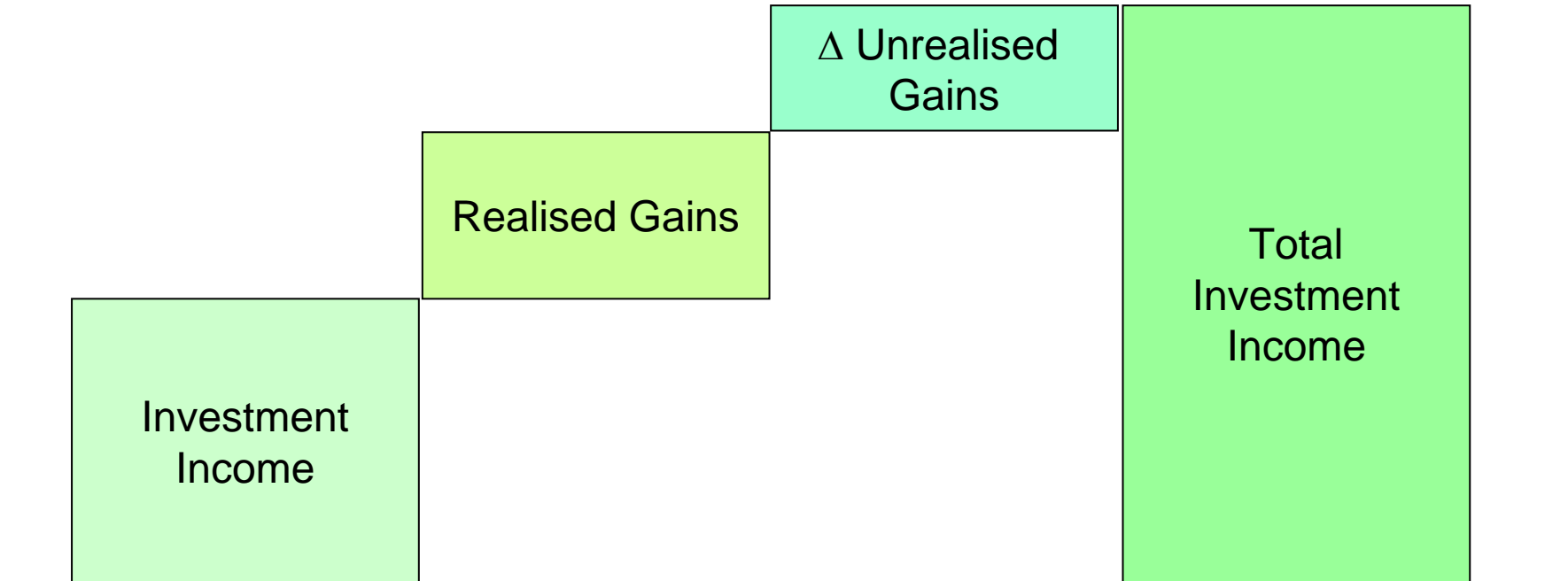
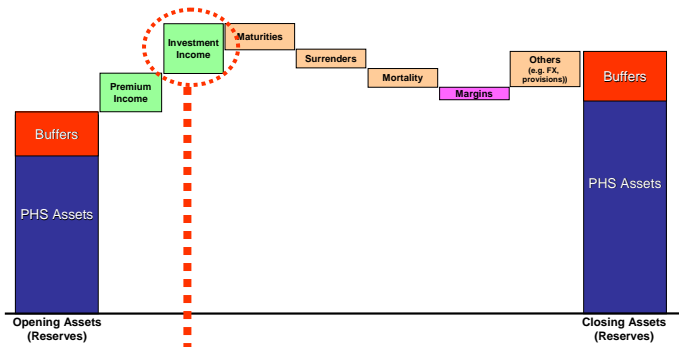
# Asset Development and Margin Analysis



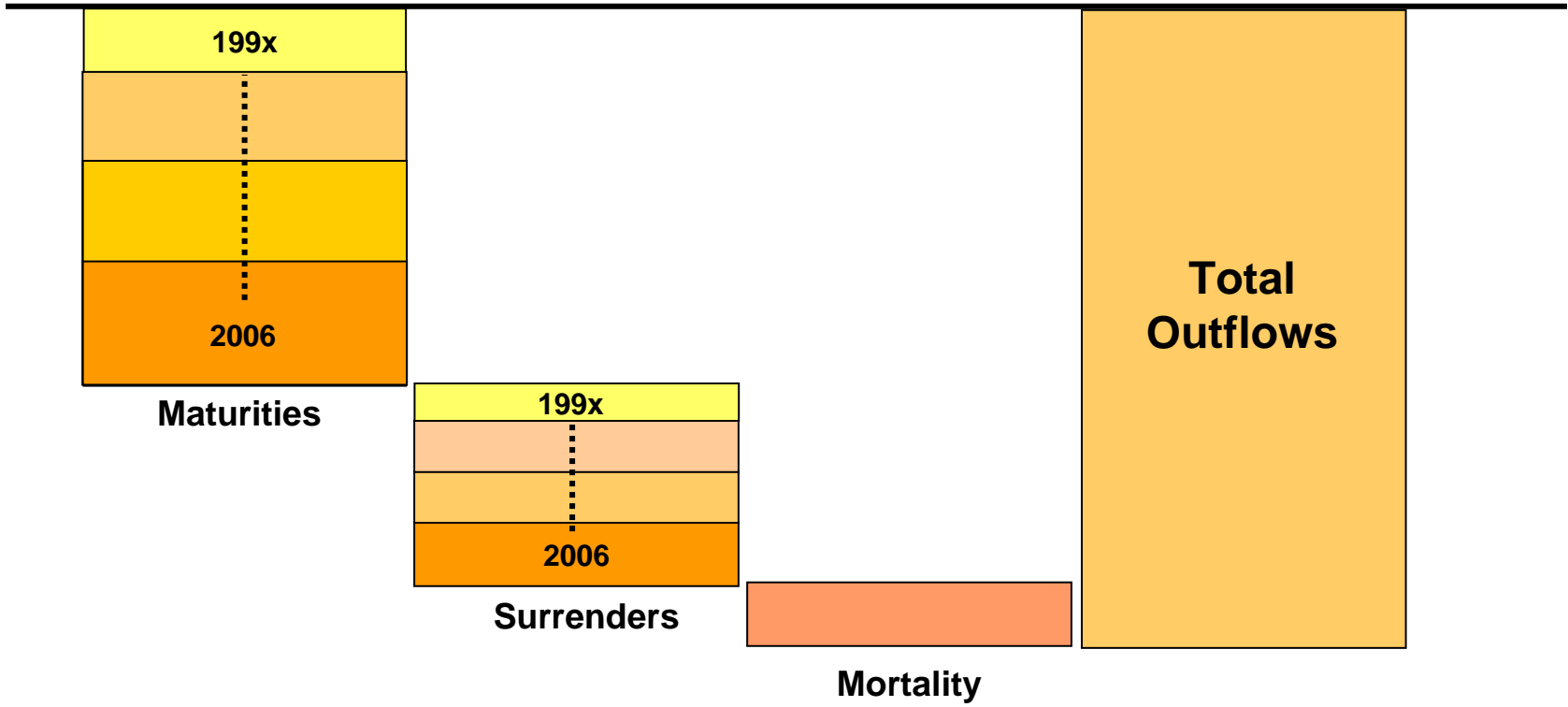
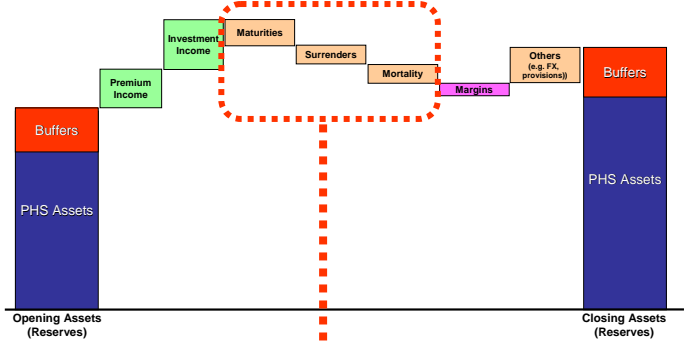
# Inflow Details (1)



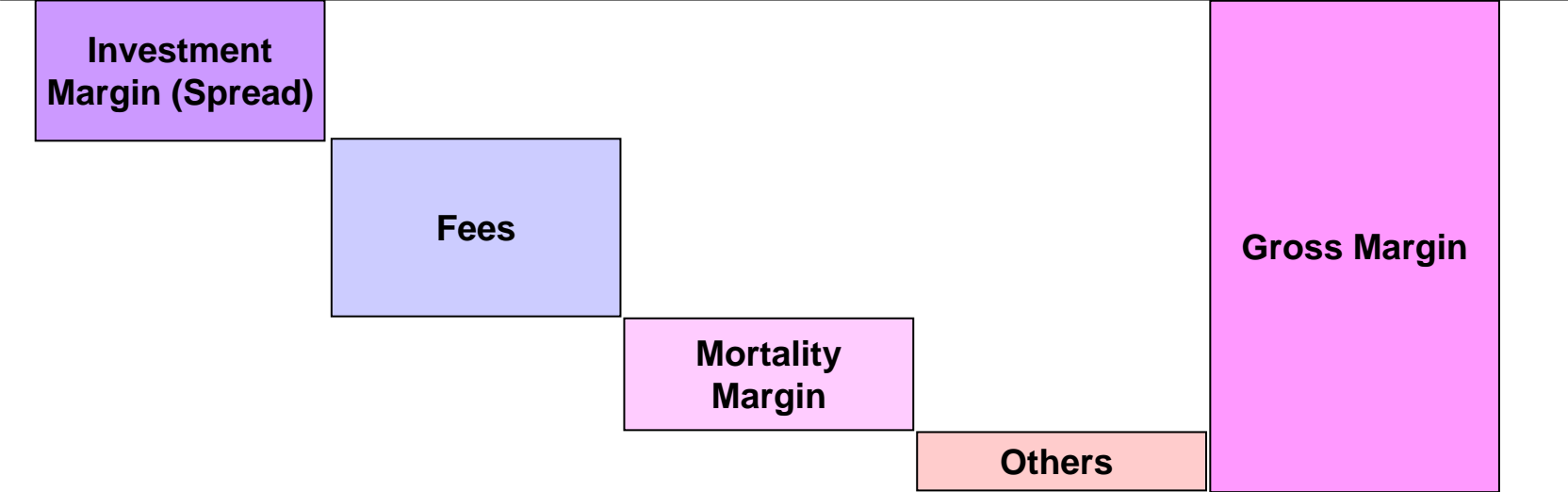
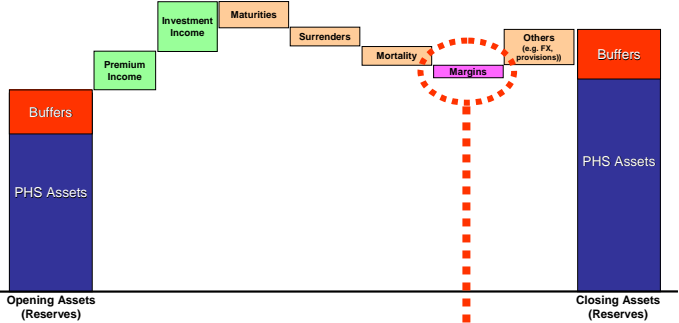
# Inflow Details (2)



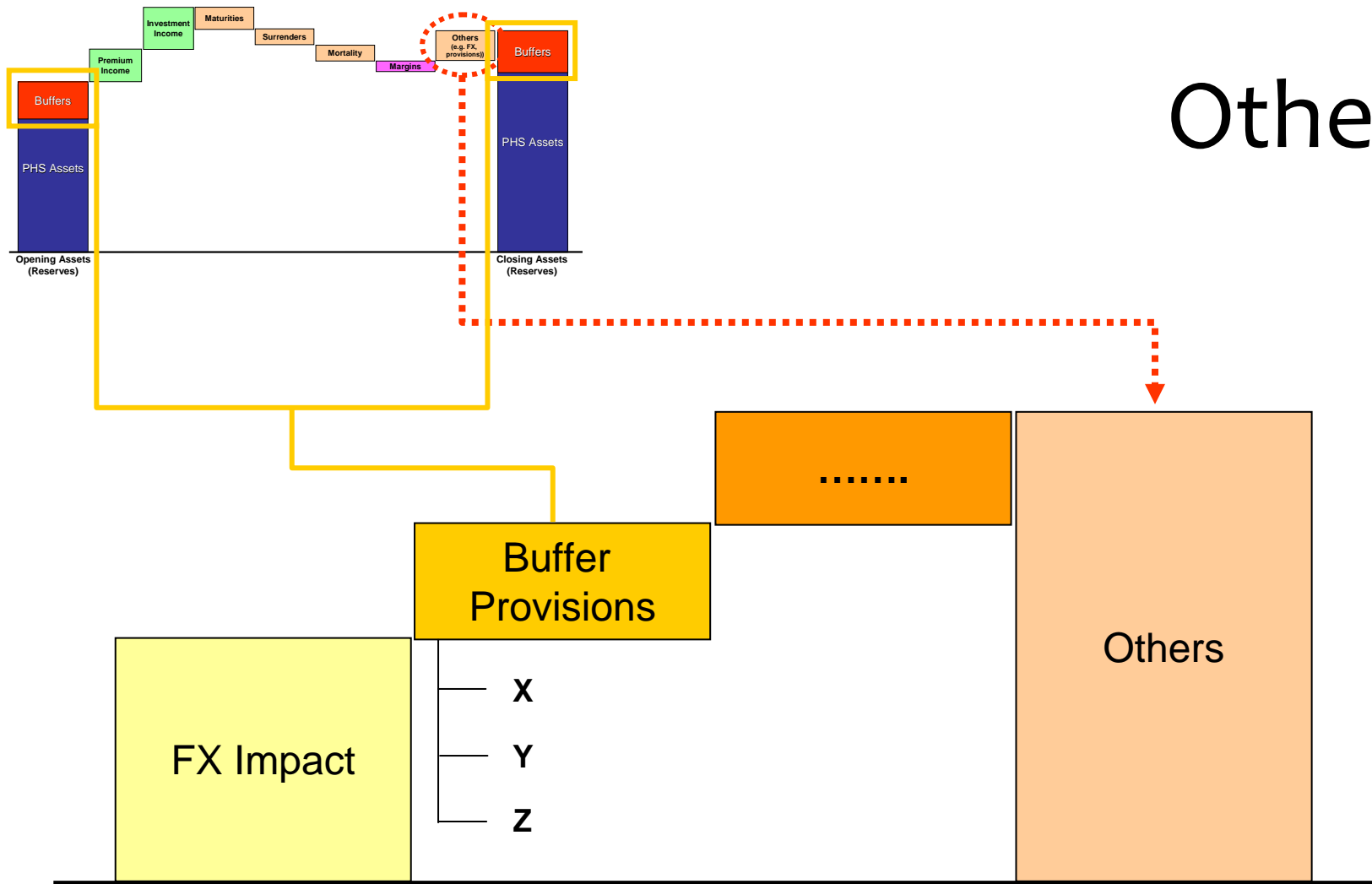
# Outflow Details



# Gross Margin



# Others



# Asset Development and Margin Analysis

## By business line

## Translated to P&L and Balance Sheet Format

	2006
<b>Opening Assets</b>	<b>100,000</b>
- Invested Assets	85,000
- Buffer	15,000
<b>Premium income</b>	<b>17,200</b>
- Premium Income (net renewals)	10,000
- Renewal (before surrenders and lapses)	15,500
- Surrenders	(3,000)
- Lapses	(2,500)
- New business premiums	7,200
- Regular	1,200
- Single	6,000
<b>Total Investment Income</b>	<b>7,500</b>
- Investment income	3,000
- Realised gains	1,800
- Δ Unrealised gains	2,700
<b>Outflows</b>	<b>(9,500)</b>
- Maturities (see note 1 for vintages)	(5,000)
- Surrenders (see note 2 for vintages)	(3,500)
- Mortality (see note 3 for detailed P&L)	(1,000)
<b>Gross Margin</b>	<b>(1,900)</b>
- Investment margin (spread)	(800)
- Fees	(500)
- Mortality margin	(600)
<b>Other movements</b>	<b>4,200</b>
- FX impact	2,400
- Buffer Provisions	1,800
<b>Closing Assets</b>	<b>117,500</b>
- Invested Assets	100,700
- Buffer	16,800

	2006
Opening Reserves	100,000
Traditional	60,000
Linked	40,000
<b>Premium income</b>	<b>17,200</b>
Traditional	6,880
Linked	10,320
<b>Investment income</b>	<b>7,500</b>
Traditional	3,600
Linked	3,900
<b>Outflows</b>	<b>(9,500)</b>
Traditional	(5,225)
Linked	(4,275)
<b>Gross Margin</b>	<b>(1,900)</b>
Traditional	(1,160)
Linked	(740)
<b>Other movements</b>	<b>4,200</b>
Traditional	2,940
Linked	1,260
<b>Closing Reserves</b>	<b>117,500</b>
Traditional	67,035
Linked	50,465

	2006
Premium Income	17,200
Investment income	7,500
<b>Claims Incurred</b>	<b>(27,000)</b>
- Paid	(9,500)
- Reserving	(17,500)
<b>Others</b>	<b>4,200</b>
<b>Gross margin (pre-tax)</b>	<b>1,900</b>
<b>Expenses (pre-DAC)</b>	<b>-665</b>
- Acquisition costs	-399
- Administrative expenses	-266
<b>Investment income on tangible capital</b>	<b>350</b>
<b>Pre-tax profit</b>	<b>1,585</b>
Taxation	-476
<b>Net profit</b>	<b>1,110</b>
<b>Shareholders equity (tangible)</b>	<b>7000</b>
<b>Reserves</b>	<b>117,500</b>
<b>Opening Value at Risk</b>	<b>4200</b>
- Market Risk	1470
- Interest Rate Risk	1680
- Mortality Risk	126
- Longevity Risk	924
<b>Closing Value at Risk</b>	<b>5875</b>
- Market Risk	2174
- Interest Rate Risk	2233
- Mortality Risk	176
- Longevity Risk	1293



# Non Life

# How do they make money?

## Cost Totals and Statistics

Total Production/Purchase Costs	\$4,800	\$4,800	\$4,800	\$4,800	\$4,800	\$4,800	\$4,800	\$4,800	\$4,800	\$4,800
Cost Statistics										
Beginning Inventory Unit Cost	\$10.00	\$10.57	\$10.95	\$11.27	\$11.54	\$11.74	\$11.85	\$11.90	\$11.93	\$11.95
Produced/Purchased Unit Cost	\$12.00	\$12.00	\$12.00	\$12.00	\$12.00	\$12.00	\$12.00	\$12.00	\$12.00	\$12.00
Weighted Average Unit Cost	\$10.57	\$10.95	\$11.27	\$11.54	\$11.74	\$11.85	\$11.90	\$11.93	\$11.95	\$11.97

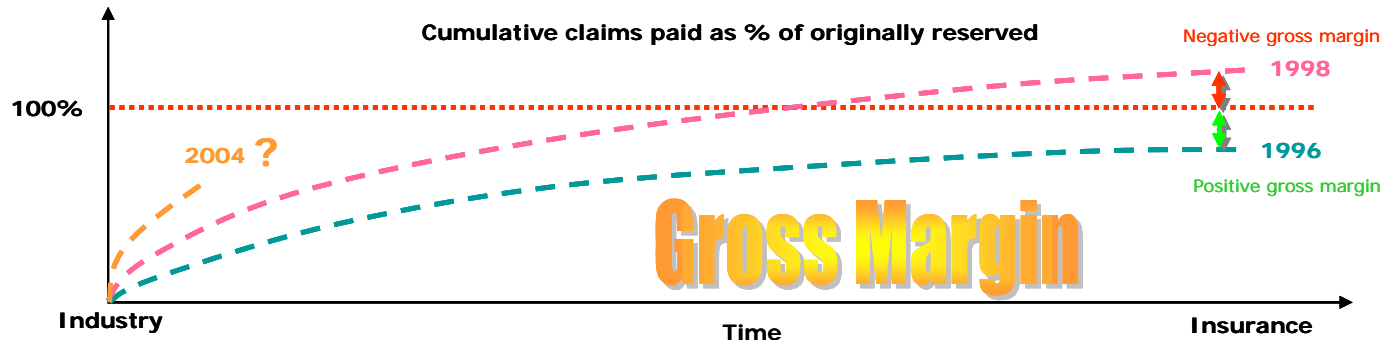
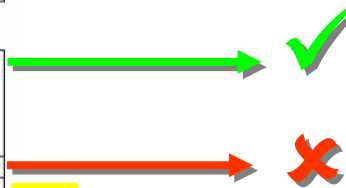
## Sales and Gross Margin Forecast

Total Sales	\$7,500	\$15,000	\$15,000	\$15,000	\$7,500	\$7,500	\$7,500	\$7,500	\$7,500	\$7,500
Less:										
Cost of Goods Sold	\$3,171	\$6,571	\$6,765	\$6,923	\$3,523	\$3,554	\$3,571	\$3,580	\$3,586	\$3,590
Other Variable Costs	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0	\$0
Total Cost of Sales	\$3,171	\$6,571	\$6,765	\$6,923	\$3,523	\$3,554	\$3,571	\$3,580	\$3,586	\$3,590
Gross Sales Margin	\$4,329	\$8,429	\$8,235	\$8,077	\$3,977	\$3,946	\$3,929	\$3,920	\$3,914	\$3,910

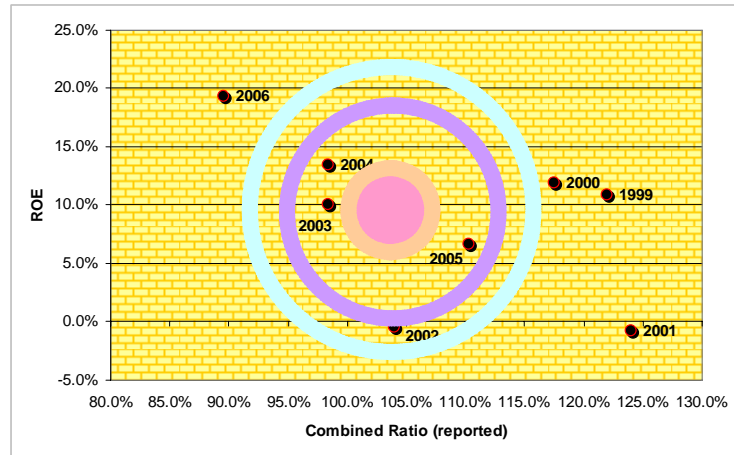
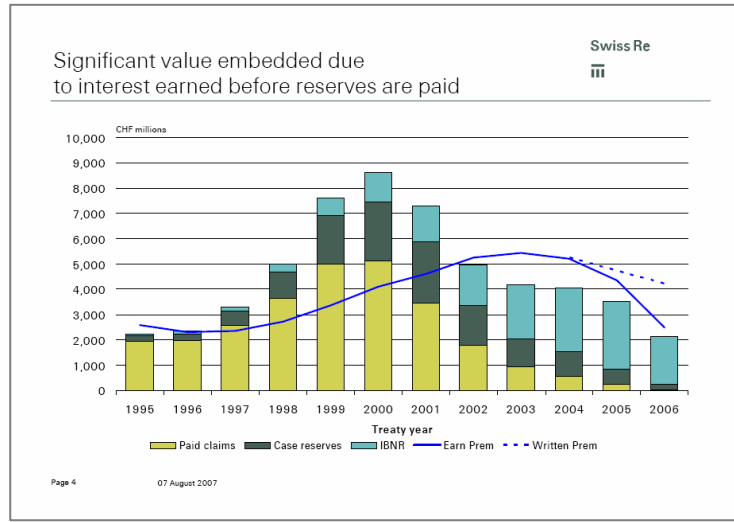
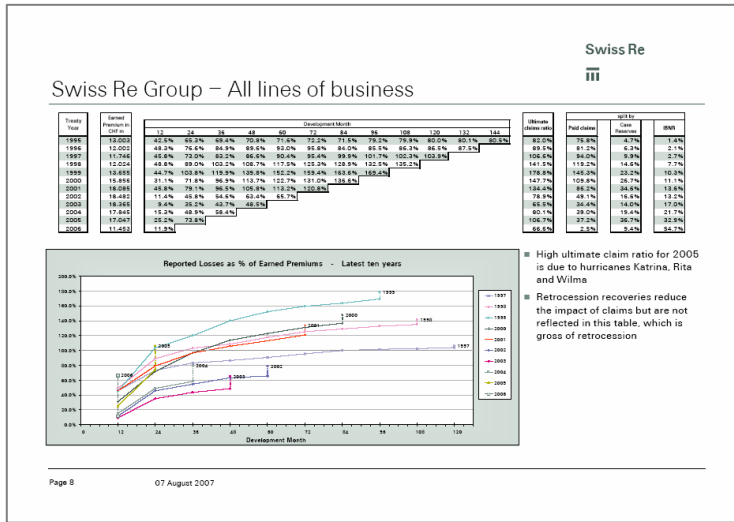
## Inventory Forecast

Inventory Changes--Units										
Beginning Units on Hand	1,000	1,100	900	700	500	600	700	800	900	1,000
Plus: Units Produced/Purchased	400	400	400	400	400	400	400	400	400	400
Less: Units Sold	300	600	600	600	300	300	300	300	300	300
Ending Units on Hand	1,100	900	700	500	600	700	800	900	1,000	1,100
Inventory Changes--Dollars										
Beginning Dollars on Hand	\$10,000	\$11,629	\$9,857	\$7,892	\$5,769	\$7,046	\$8,292	\$9,522	\$10,741	\$11,955
Plus: Dollars Produced/Purchased	\$4,800	\$4,800	\$4,800	\$4,800	\$4,800	\$4,800	\$4,800	\$4,800	\$4,800	\$4,800
Less: Dollars Sold	\$3,171	\$6,571	\$6,765	\$6,923	\$3,523	\$3,554	\$3,571	\$3,580	\$3,586	\$3,590
Ending Dollars on Hand	\$11,629	\$9,857	\$7,892	\$5,769	\$7,046	\$8,292	\$9,522	\$10,741	\$11,955	\$13,164

What is the cost of sales?  
When does it crystallise?

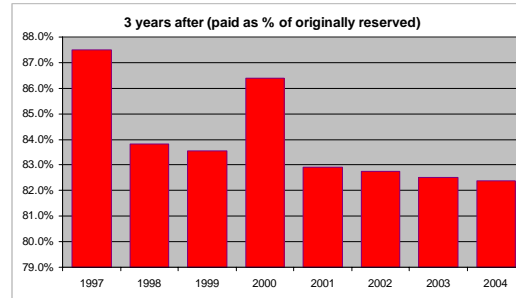


# Gross Margin Crystallisation



# Monitoring the “pots of money”

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	Consolidated FY 2007
<b>T-9</b>												
Premiums (net of expenses)	0	10500										
Claims paid	-500	-8400										
Reserving	500	-2100										
Investment income	75	105										
Margin	75	105										
Reserves	1500	2100										
<b>T-8</b>												
Premiums (net of expenses)	0	0	11025									
Claims paid	-250	-220	-8820									
Reserving	250	220	-2205									
Investment income	63	94	110									
Margin	63	94	110									
Reserves	1250	1880	2205									
<b>T-7</b>												
Premiums (net of expenses)	0	0	0	11576								
Claims paid	-150	-180	-210	-3261								
Reserving	150	180	210	-2315								
Investment income	55	85	100	116								
Margin	55	85	100	116								
Reserves	1100	1700	1995	2315								
<b>T-6</b>												
Premiums (net of expenses)	0	0	0	0	12155							
Claims paid	-100	-110	-180	-550	-9724							
Reserving	100	110	180	550	-2431							
Investment income	50	80	91	88	122							
Margin	50	80	91	88	122							
Reserves	1000	1590	1815	1765	2431							
<b>T-5</b>												
Premiums (net of expenses)	0	0	0	0	0	12763						
Claims paid	-80	-90	-105	-190	-205	-10210						
Reserving	80	90	105	190	205	-2553						
Investment income	46	75	86	79	111	128						
Margin	46	75	86	79	111	128						
Reserves	920	1500	1710	1575	2226	2553						
<b>T-4</b>												
Premiums (net of expenses)	0	0	0	0	0	0	13401					
Claims paid	-50	-80	-100	-150	-150	-200	-10721					
Reserving	50	80	100	150	150	200	-2680					
Investment income	44	72	81	71	104	118	134					
Margin	44	72	81	71	104	118	134					
Reserves	870	1440	1610	1425	2076	2353	2680					
<b>T-3</b>												
Premiums (net of expenses)	0	0	0	0	0	0	0	14071				
Claims paid	-50	-50	-70	-120	-120	-150	-190	-11257				
Reserving	50	50	70	120	120	150	190	-2814				
Investment income	41	70	77	65	98	110	125	141				
Margin	41	70	77	65	98	110	125	141				
Reserves	820	1390	1540	1305	1956	2203	2490	2814				
<b>T-2</b>												
Premiums (net of expenses)	0	0	0	0	0	0	0	14775				
Claims paid	-10	-45	-40	-100	-80	-125	-145	-185	-11620			
Reserving	10	45	40	100	80	125	145	185	-2955			
Investment income	41	67	75	60	94	104	117	131	148			
Margin	41	67	75	60	94	104	117	131	148			
Reserves	810	1345	1500	1205	1876	2078	2345	2629	2955			
<b>T-1</b>												
Premiums (net of expenses)	0	0	0	0	0	0	0	0	15513			
Claims paid	-10	-5	-40	-60	-70	-75	-110	-150	-195	-12411		
Reserving	10	5	40	60	70	75	110	150	195	-3103		
Investment income	40	67	73	57	90	100	112	124	138	155		
Margin	40	67	73	57	90	100	112	124	138	155		
Reserves	800	1340	1460	1145	1806	2003	2235	2479	2760	3103		
<b>T</b>												
Premiums (net of expenses)	0	0	0	0	0	0	0	0	0	16289		16289
Claims paid	-10	0	-15	-60	-30	-60	-80	-130	-160	-210	-13031	-13786
Reserving	10	0	15	60	30	60	80	130	160	210	-3258	-2503
Investment income	40	67	72	54	89	97	108	117	130	145	163	1082
Margin	40	67	72	54	89	97	108	117	130	145	163	1082
Reserves	790	1340	1445	1085	1776	1943	2155	2349	2600	2893	3258	21634
Total	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	
Claims Paid	9210	9160	9580	10491	10379	10820	11246	11722	12175	12621	13031	
% of originally reserved	92.1%	87.2%	86.9%	90.6%	85.4%	84.8%	83.9%	83.3%	82.4%	81.4%	80.0%	
Residual reserves as % of originally reserved	7.9%	12.8%	13.1%	9.4%	14.6%	15.2%	16.1%	16.7%	17.6%	18.6%	20.0%	



- What is the ultimate margin on the business written?

- The business is cyclical but the results “melt” different parts of the cycle.

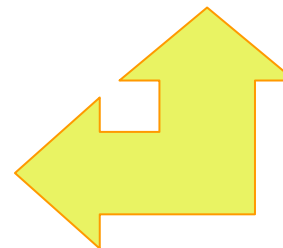
Disclosure should allow a “generational” visibility of the business.

- Would it make sense to publish development by accident year by business line?

- Profit appropriation on running liabilities...is it a still picture or a moving target?

<b>Profit and loss</b>	<b>2007</b>
Premiums including expenses	19163
Expenses (administrative and commissions)	-2875
Premiums excluding expenses	16289
Claims Incurred (paid + reserving)	-16289
Underwriting result	0
Investment income	1082
<b>Insurance Margin</b>	<b>1082</b>
Combined ratio	100.0%
Loss ratio	85.0%
Expense ratio	15.0%
<b>Return on capital employed</b>	<b>431</b>
Pre-tax profit	1513
Taxation	-454
<b>Net income</b>	<b>1059</b>
- ROE	<b>12%</b>
<b>Balance Sheet</b>	<b>2007</b>
Claims reserves	21634
Allocated capital	8624

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# Getting Closer to Other Industries

- **More visibility is required to understand the ultimate cost of risk and margin crystallisation.**
- **On the life front, asset development and margin analysis on a cash basis is needed to understand how the life operations make money.**
- **Don't mix financial reporting with risk reporting – this is a recipe for disaster. Learn from the banks.**
- **Don't use one size fits all for disclosure. Different divisions may require different reporting formats – think on how to model the money-making process of that particular division.**
- **Produce cash disclosure and capital absorption criteria. This helps to estimate free cash flows.**
- **Make all of this disclosure part of your accounts (accountants are legally bound by their disclosures).**
- **90% of investors are not insurance/reinsurance experts.**
- **Insurance/reinsurance represent around 5% of global market capitalisation. Would you take a PhD for 5% of your universe? Make it simple, make it understandable.**