

## Changes Abroad, Challenges at Home

**A** PRESIDENTIAL ELECTION YEAR is always an exciting time to be in Washington. All eyes focus either warily or hopefully on the possible changes to the public policy landscape. It's also an exciting time for the Academy as the relevance of our priorities is greatly affected by a new administration and a new session of Congress.

With all the focus on national politics, it's often hard for any of us—but particularly for those of us working and living in Washington—to focus on anything else. But that would be shortsighted. Beyond our borders, there is a wide range of international developments emerging that will have a tremendous impact on the actuarial profession.

Perhaps the broadest and most visible international

issue for actuaries is the convergence of domestic and international accounting standards. Actuaries deal largely in numbers, so it stands to reason that any change in how numbers can be interpreted and recorded on financial statements has the potential to alter professional practices—practices that have been around, in some cases, for decades.

Convergence of accounting standards is and will continue to be a sticky issue. (“Sticky” is a technical term we policy analysts apply to the vast range of things we don't fully understand.) The momentum of the U.S. and international approaches has carried each accounting system in a different direction, and it will take a tremendous defiance of inertia to redirect those systems toward something resembling harmony. There is no accounting Rosetta stone, no basis for comparison to reconcile vastly different approaches to the common goal of accurate and useful financial reporting.

Recently, the International Accounting Standards Board (IASB) has cranked up its activity in producing new standards. One in particular, International Financial Reporting Standard (IFRS) 4, addresses how insurance contracts should be accounted for on financial statements. IFRS 4 represents the first phase of the IASB's two-phased approach to insurance contracts and essentially lays the groundwork for Phase 2, which is expected to get underway in 2005.

While Phase 1 is focused on improving disclosures—it addresses exciting things such as accounting for embedded derivatives and unbundling of insurance and deposit components for certain contracts—Phase 2 will be a broader look at applying fair value accounting to insurance contracts.

Developing a fair value approach will undoubtedly be difficult. Conceptually, the fair value of an insurance contract is the meeting of what the seller is willing to accept and what the buyer is willing to pay. Determining that real cost, however, depends on a



**ETHAN SONNICHSEN** is policy analyst, risk management and financial reporting, for the American Academy of Actuaries in Washington.

real market which, in the case of certain contracts, doesn't exist.

The IASB's U.S. counterpart, the Financial Accounting Standards Board (FASB), is working jointly with the IASB and has recently taken the lead on fair value. In June 2004, FASB released a proposal, "Fair Value Measurements," to provide guidance on measuring fair value, but whether that proposal will serve as the backbone for Phase 2 of the IASB's insurance contracts project is uncertain. What is certain, however, is that a significant change to the accounting and actuarial profession is well underway.

With new international accounting standards come new requirements for those actuaries who must use them. The International Actuarial Association (IAA) is currently developing international actuarial standards of practice that relate

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directly to relevant IFRSs. The standards will provide the guidance necessary to deal with the insurance and investment contracts issued by international insurers and subject to international accounting requirements. The Academy and the Actuarial Standards Board are working closely with the IAA on this effort, and the Financial Reporting Committee will have commented on multiple drafts of the standards by the time they're finalized.

Elsewhere, outside of the accounting realm, there is international activity relating to the regulation of insurance.

The International Association of Insurance Supervisors (IAIS), perhaps best described as the National Association of Insurance Commissioners (NAIC) of NAIC-like bodies around the world, hopes to develop a global framework for insurer capital requirements.

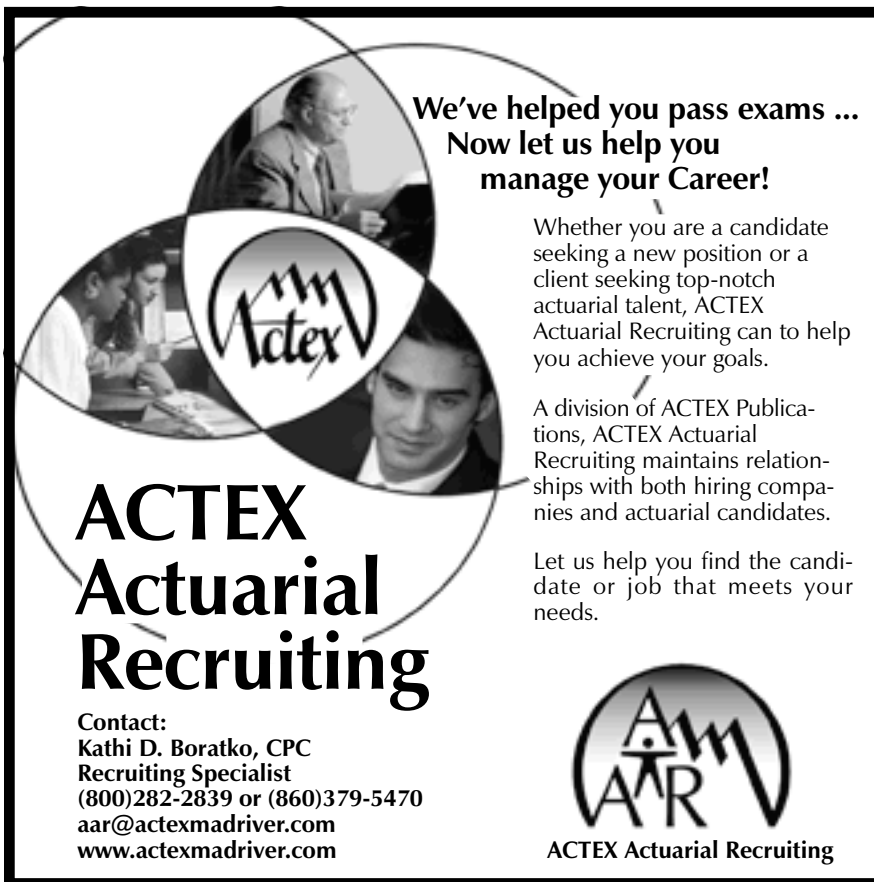
Much as the Academy often acts in technical support of the NAIC on U.S. issues, the IAA's Insurer Solvency Assessment Working Party acted in support of the IAIS in this international effort and has developed an educational research paper, "A Global Framework for Insurer Solvency Assessment," to serve as a risk-focused view of such a framework.

The paper outlines best practices and guiding principles for a supervisory system to ensure adequate funds to cover exposure to risks, and discusses various mechanisms for identifying and quantifying those risks. The IAIS and NAIC are both reviewing the document, and it will likely play a significant role as the IAIS works toward a global standard for capital requirements.

This collection of issues is merely the tip of the actuarial iceberg, but the Academy has commented on, or been directly engaged in all of them. As the pace of international developments quickens, the Academy's involvement, both individually and through membership in the IAA, has also increased.

The IAA is in the unenviable position of being the first responder for the actuarial profession on most international developments, and its work is imperative. The U.S. actuarial profession, however, has a stake in many of these international developments, whether it welcomes that involvement or not. As the U.S. profession's voice, the Academy has an obligation to participate.

So as the U.S. political environment adapts to a new season and the Academy adapts to new priorities, we need to keep one eye always on the horizon. Changes abroad will lead to challenges at home, but if the Academy and its allies continue their efforts, the actuarial profession is well prepared to meet them.



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