ICP 26: Information, Disclosure, and Transparency toward the Market

Basic-level Module
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About the Core Curriculum

A financially sound insurance sector contributes to economic growth and well-being by supporting the management of risk, allocation of resources, and mobilization of long-term savings. The insurance core principles (ICPs), developed by the International Association of Insurance Supervisors (IAIS), are key international standards relevant for sound financial systems.

Effective implementation of the ICPs requires skilled and knowledgeable insurance supervisors. Recognizing this need, the World Bank and the IAIS partnered in 2002 to develop a “core curriculum” for insurance supervisors. The Core Curriculum Project, funded and supported by various sources, accelerates the learning process of both new and experienced supervisors. The ICPs provide the structure for the core curriculum, which consists of a set of modules that summarize the most relevant aspects of each topic, focus on the practical application of supervisory concepts, and cross-reference existing literature.

The core curriculum is designed to help those studying it to:

- Recognize the risks that arise from insurance operations
- Know the techniques and tools used by private and public sector professionals
- Identify, measure, and manage these risks
- Operate effectively within a supervisory organization
- Understand the ICPs and other IAIS principles, standards, and guidance
- Recommend techniques and tools to help a particular jurisdiction observe the ICPs and other IAIS principles, standards, and guidance
- Identify the constraints and identify and prioritize supervisory techniques and tools to best manage the existing risks in light of these constraints.
Welcome to the ICP 26: Information, disclosure, and transparency toward the market module. This is a basic-level module on information, disclosure, and transparency toward the market that does not require specific prior knowledge of this topic. The module should be useful to either a new insurance supervisor or an experienced supervisor who has not dealt extensively with the topic or is simply seeking to refresh and update knowledge.

Start by reviewing the objectives, which will give you an idea of what a person will learn as a result of studying the module, and answer the questions in the pretest to help gauge prior knowledge of the topic. Then proceed to study the module either on an independent, self-study basis or in the context of a seminar or workshop. The amount of time required to study the module on a self-study basis will vary, but it is best addressed over a short period of time, broken into sessions on parts if desired.

To help you engage and involve yourself in the topic, we have interspersed the module with a number of hands-on activities for you to complete. These are intended to provide a checkpoint from time to time so that you can absorb and understand the material more readily. You are encouraged to complete each of these activities before proceeding with the next section of the module. An answer key in appendix II sets out some of the points that you might consider when completing the exercises. You will also find questions dealing with the local situation and related to practices in your jurisdiction. These are intended to help you apply the material in this module to your local circumstances. If you are working with others on this module, develop the answers through discussion and cooperative work methods. As appropriate to your experience and role, consider life, health, and non-life insurance separately. Since these responses will vary by jurisdiction, the answer key suggests where you might look for the answers.
As a result of studying the material in this module, you will be able to do the following:

1. Discuss the role of disclosure in maintaining efficient, fair, safe, and stable insurance markets
2. Describe the potential direct and indirect costs of disclosure that must be weighed against its benefits
3. Identify the various stakeholders that may be interested in information regarding the position of an insurer and the risk to which it is subject
4. Explain how the interests of a policyholder may differ from those of a shareholder and the implications of such differences on the types of information they need
5. Justify the need for disclosure by insurers, in response to the contention that “most policyholders are either uninterested in the information or unable to understand it”
6. Explain the types of information contained in the audited financial statements, the notes to such statements, management’s discussion, and analysis in an insurer’s annual report
7. Describe the types of quantitative and qualitative information that could be disclosed by an insurer to give stakeholders a view of their business activities, financial performance, financial position, risk exposures, and corporate governance
8. Explain the role of the supervisory authority in the disclosure process
9. Enumerate the criteria that can be used to evaluate the usefulness of information disclosed by insurers
10. Describe the various communication vehicles that can be used by an insurer to disclose information and illustrate the types of information that might appropriately be communicated through each
11. Review the information disclosed by a particular insurer and assess its completeness and usefulness
12. Summarize the requirements of ICP 26.
Pretest

Before studying this module on information, disclosure, and transparency toward the market, answer the following questions. The questions are designed to help you gauge your existing knowledge of this topic. An answer key is presented in appendix II at the end of the module.

For questions 1 through 4, consider the statements made and indicate whether you consider each to be appropriate and reasonable or inappropriate and unreasonable. Discuss the reasons for your conclusion in each case.

1. Disclosure of information is a key pillar of the supervisory framework.

2. The supervisory authority should confirm information disclosed by insurers.

3. When a piece of information has been disclosed, it can be assumed to be meaningful to all recipients.

4. The level of disclosure by insurers to the market should be the same as for other commercial entities.

5. Identify three cases in your recent experience in which lack of disclosure or inappropriate disclosure resulted in adverse outcomes. What steps would you take to prevent these situations from recurring?
ICP 26: Information, Disclosure, and Transparency toward the Market

Basic-level Module

A. Introduction

This module focuses on IAIS Insurance Core Principle (ICP) 26: Information, disclosure, and transparency toward the market. Other principles, which are presented in IAIS (2003b), relate to ICP 26, including, in particular:

- ICP 9 on corporate governance
- ICP 12 on reporting to supervisors and offsite monitoring
- ICP 13 on onsite inspection
- ICP 24 on intermediaries (to some extent)
- ICP 25 on consumer protection
- ICP 27 on fraud
- ICP 28 on anti-money laundering and combating the financing of terrorism.

The need for appropriate disclosure to the supervisory authority is implicit in the principles addressing prudential requirements (ICPs 18–23). In many jurisdictions where the concept of a financial condition report is established, these requirements are addressed in the content of the report. The importance to supervisors of the financial condition report is highlighted in IAIS (2003a), recommendations 15, 16, and 17.

This module focuses more on the processes of disclosure than on the content of the information disclosed. Other ICPs address the specifics of the information to be disclosed. For example, ICP 25 addresses consumer protection and requires “provision of timely, complete, and relevant information to [insurance] consumers,” so these other ICPs are the appropriate place to look for details on the information to disclose.
Disclosure processes should evolve in line with changing needs and available tools. For example, in many jurisdictions, unit-linked products are gaining a substantial market share, and these products have particular characteristics that need to be brought to the attention of consumers. Each jurisdiction will need to consider how best to approach this, reflecting such things as the level of education of its consumers, the sophistication of intermediaries, and the capacity of the insurers providing the products. The Internet—both the World Wide Web and e-mail—can have a profound impact on how information can be disclosed. For example, in some countries electronic signatures in some form are now legally acceptable (see IAIS 2004b).

Underlying this module is the basic need for effective communication between two or more parties. For communication to be effective, it is important for the message of the sender to be received and understood by the recipient. This implies that both senders and receivers are competent and share common language and concepts. In the area of insurance, there can be major and ongoing information asymmetries that threaten this underlying requirement. There is little point, for example, in providing a technical actuarial report to all prospective purchasers of insurance coverage because, in all likelihood, most recipients of the information will have no idea what it means. While in a formal sense the information has been disclosed, in any meaningful sense disclosure was a waste of time and effort, since the information is unintelligible to the recipient. This does not imply that the actuarial report in question is a “bad” report, just that it is used inappropriately. The counterpoint to this example is the contention that “I did not read the information” is an unacceptable defense. These comments highlight the responsibilities and expectations placed on both the senders and recipients of information. These responsibilities and expectations will evolve as the relative capacities of senders and receivers change. Supervisors have an important role to play in assessing and developing these responsibilities and expectations.

The ICPs are generally applicable to both life and non-life insurance, as is the discussion in this module, unless specifically indicated otherwise. While written in the context of insurance, this module is applicable in both the insurance and reinsurance contexts, unless specifically indicated otherwise.

Many terms take on specific meanings in the context of insurance. A useful reference in this context is the IAIS Glossary of Terms (IAIS 2006a). Where relevant, further terms are defined in the text, and further references are provided.

This module identifies principles and issues that relate to specific topics. The intent is to provide an insight into the issues and their possible consequences. While this process should raise questions, it does not necessarily propose unique solutions. Solutions in practice depend on the specific environment and context in which the topic arises. However, the set of issues to consider in addressing these topics remains fairly constant.
Disclosure as a supervisory pillar

The IAIS has emphasized the importance of providing markets with relevant information and using market discipline as an adjunct to supervisory processes. In recent papers, the IAIS has identified a high-level model for insurance supervision (IAIS 2005a, 2006b). This structure has three levels: preconditions, regulatory requirements, and supervisory action. In the level of regulatory requirements, there are three blocks: financial, governance, and market conduct. As disclosure requirements may pertain to each of these three blocks, the IAIS framework incorporates public disclosure requirements into them (IAIS 2005b). This approach is compatible with the Basel II approach currently being implemented globally in the banking sector, which has disclosure as one of its three major regulatory pillars (BCBS 2004).

In line with earlier comments concerning the distinction between messages sent as opposed to messages received, while supervisors can play a role in assessing whether disclosure requirements have been met, they cannot ensure that the recipients of the disclosed information will use it as expected. In an efficient marketplace, disclosure is expected to provide an effective basis for market discipline. In markets that are not yet efficient, disclosure requirements may assist in improving efficiency. In some circumstances, supervisory authorities may need to consider further actions to support the disclosure of information.

ICP 26 states,

The supervisory authority requires insurers to disclose relevant information on a timely basis in order to give stakeholders a clear view of their business activities and financial position and to facilitate the understanding of the risks to which they are exposed.

The full text of ICP 26, including explanatory notes and assessment criteria, is provided in appendix I. To support the ICPs, the IAIS has prepared principles, standards, and guidance papers. These documents, several of which deal specifically with disclosure, should be considered as an integrated body of work.

In summary, disclosure to the market is a vital component of the supervisory process and, in an efficient marketplace, is expected to be an effective means of market discipline.
Exercises

1. To what extent do insurers in your jurisdiction satisfy essential criteria a–d of ICP 26?

2. To what extent does your supervisory authority have in place methodologies, processes, and expertise to assess the practices of insurers operating in your jurisdiction with regard to the essential criteria of ICP 26?

3. To the extent that an insurer does not satisfy some of the essential criteria of ICP 26, what powers and practices does your supervisory authority have in place to direct and ensure compliance with these criteria?
B. The broader context

In this section, some broader contextual issues are considered, including the distinctions between disclosure and transparency, data and information, and disclosure to the public versus disclosure to supervisory authorities. The role of perception, the differing interests of various stakeholders, and the need to adapt requirements to the particular situation of a jurisdiction are discussed as well.

**Disclosure versus transparency**

ICP 26 includes both the words “disclosure” and “transparency.” These concepts are explored further here.

The term “disclosure” describes the provision of information. In particular, disclosure requirements generally specify the minimum information to be provided. This does not, of itself, consider whether recipients can use the information effectively. Disclosure requirements are externally imposed and sometimes not integrated into internal management reporting within insurers.

The term “transparency” describes how the disclosure is done, with an emphasis on whether the user or recipient of the information is able to understand and use the information. The change in perspective from provider to receiver of information is important, as it governs the effectiveness of the disclosure process. While this implies that the provider of the information needs to understand the capacity of the recipients to assess the information, it also places responsibility on the recipients to make an effort to understand the information provided. Nevertheless, the provider should make every effort to make information convenient and easy to understand.

Transparency implies that the recipients of the information can gain some understanding of the “why” and “how” behind the data reported, not just the quantum of the data provided. This understanding is important, as understanding the drivers of changes in results from one period to the next is critical to understanding the trends and conclusions that may emerge, as well as enhancing the assessment of their effects. Trends that appear from high-level disclosed data do not necessarily have the “obvious” drivers supporting them. For example, an insurer may report a decline in total expenses not because efficiencies have improved but simply because necessary spending has been deferred. In this case, transparency should provide insight into the drivers of the change.

A feature of disclosed information that may assist with transparency is the format in which the information is disclosed. Supervisory authorities can have a significant role to play in specifying such formats. The advantage of specified formats is that there is consistency of information, both over time and among insurers. The risk that the supervisory authority takes in specifying formats is that such specifications can prohibit further disclosure, enable insurers to “game the system,” and, in some cases, remove
the possibility for further improvements and experimentation. Supervisory authorities should be aware of such risks.

The IAIS has expressed the opinion, “Disclosure to the public of relevant, reliable, and timely information is critical to the operation of a sound market and to achieving the aims of transparency, comparability, and convergence” (see IAIS 2005d). That is, disclosure is a necessary precursor to transparency, and transparency is a necessary precursor to comparability among insurers, the insurance sectors of various jurisdictions, and insurers and other financial institutions.

Two specific IAIS standards on public disclosure have been adopted to date, with more anticipated. They are Standard 9: Disclosures Concerning Technical Performance and Risks for Non-life Insurers and Reinsurers and Standard 11: Disclosures Concerning Investment Risks and Performance for Insurers and Reinsurers (IAIS 2004c, 2005c). Also relevant is Guidance 11: Risk Transfer, Disclosure, and Analysis of Finite Reinsurance (IAIS 2005a).

In summary, disclosure deals with what information is provided and transparency with how the information is provided so that it becomes meaningful.

**Data versus information**

There is an important distinction between data and information. In this context, information means the results of applying analysis and synthesis to the data provided. The process of analysis requires skill and experience to be able to assess and interpret the data and then draw conclusions or identify emerging issues. This process can be difficult, and it is not always possible to draw clear conclusions; rather, further questions may be prompted. Supervisors should not expect that, in all cases, simple rules can be derived to apply mechanically to data and generate analytic results. Both the quantitative and qualitative aspects should be recognized in the analyses, and interpretations need to be reached with a combination of “art and science.”

These comments apply equally to supervisors and to other users of disclosed data.

**Public versus supervisory disclosure**

Insurers operate in an environment in which multiple influences are at work. While a key influence is the supervisory regime, other important influences include, for example, general legal requirements as applicable to all business entities, general-purpose accounting standards, taxation requirements, and requirements of bourses (stock exchanges), for listed insurers. Typically, these other influences also have reporting requirements, and the resulting reports may be publicly available. The purposes for which these reports, publicly available or not, are made differ from insurance supervisory purposes, and care needs to be taken in using or interpreting them in a supervisory context.
Moreover, the insurance supervisor typically has little or no direct control over these additional reporting requirements.

At least some of the information received by supervisory authorities is also confidential and intended, among other things, to assist the supervisor in assessing the long-term solvency of the insurer. It is not appropriate to make this confidential information publicly available, as it may include commercially sensitive information. The financial condition report is a key example of confidential information that is disclosed to the supervisory authority.

Supervisors should be aware of the need, where practical, to ensure that the financial information required of insurers for supervisory purposes is consistent with the financial information required for other purposes. Inconsistent requirements impose additional costs on insurers, and inconsistent publicly reported information tends to confuse stakeholders. However, supervisors need to be aware that they have a specific responsibility for setting prudential standards and maintaining stable and solvent insurance industries.

In line with the essential criteria outlined in ICP 26, this module focuses on publicly disclosed information, although the principles outlined remain applicable to confidential reporting as well.

The supervisory authority can play a role in providing the markets with public information based on statistics it has gathered and analyses it has carried out. The supervisory authority is uniquely placed to assess comparability among the insurers it supervises, given the data it has at hand, and so potentially has a responsibility to provide the industry with relevant feedback regarding emerging trends and issues. In this role, the supervisory authority needs to balance the desire to receive information with the need to preserve the integrity, confidentiality where appropriate, and effectiveness of the prudential supervisory process. A specific example of this balance is given in IAIS (2004c) in the discussion on reporting of stress tests. The supervisory authority also needs to consider whether other reputable and reliable sources of similar information are available to stakeholders. If not, it may need to take a more active role in the collection and dissemination of information.

The supervisory authority has multiple roles in the disclosure process. It needs to ensure that appropriate information is disclosed by the entities it supervises. Separately, it has a role in the disclosure of appropriate public information regarding the industry. This latter role may be direct or indirect.

**Role of perception**

The credibility of the information disclosed is important. The providers of information, whether or not it is disclosed to the public, should take steps to ensure its integrity and correctness to an appropriate level.
Supervisors should be keenly aware of these issues in terms of the quality and consistency of information—confidential or public—received from the insurers they supervise. Most likely, the supervisor first performs a set of consistency checks, internal to the data set, relative to prior data received, and relative to information gathered from other sources. In some instances, issues may arise regarding the capacity of the supervisory authority to check and analyze the data received. The supervisory authority needs to identify and address such limitations in order to avoid damaging its reputation.

Supervisors are generally well aware of both the importance of their reputation with the industry they supervise as well as with the public and the importance of managing these perceptions. As a consequence, supervisory authorities need to have the powers and the will to enforce appropriate penalties for the disclosure of incorrect or misleading information and then to require corrected information.

Given the long-term nature of much insurance, the fiduciary and trustee duties of insurers are significant with regard to the management and operations of insurance entities. This highlights the importance of public confidence, in which there may be a significant component of perception, as distinct from information or views, of either the supervisory authority or the industry.

**Disclosure stakeholders**

For there to be a need for disclosure, there have to be parties to whom it is relevant to disclose information. This presumes that at least two parties are involved and maybe more. For effective communication, both distributors of information and receivers of information need to be on same wavelength.

The pursuit of both the disclosures to be considered and the level at which those disclosures should be made requires identifying the stakeholders and their relative roles and needs. In principle, each relevant pairing of stakeholders should be considered, recognizing that each pairing has different needs, objectives, and capabilities.

A stakeholder matrix is useful for this analysis. Figure 1 provides a partially completed example of a stakeholder matrix. Each cell can be analyzed, and many are addressed in the various ICPs.

The following are a number of observations about this matrix, in the context of disclosure:

**Main links considered in this module**

The main links are marked by an X in the matrix. Many other linkages are relevant to supervisors and are dealt with in other ICPs. For example,
**Figure 1. Stakeholder matrix**

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<th>Sender</th>
<th>Supervisor</th>
<th>Insurer</th>
<th>Investor</th>
<th>Intermediaries</th>
<th>Policyholders</th>
<th>Professional infrastructure</th>
<th>Market</th>
<th>Industry</th>
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- **Insurer-to-supervisor.** This includes reporting on prudential solvency requirements. See the reporting of the conclusions from ICPs 18 through 23.
- **Public-to-insurer.** This covers a broad range of issues, including the obligations of potential policyholders regarding underwriting requirements, the avoidance by insurers of identity fraud by potential employees, and the customer due diligence requirements for anti-money laundering (see ICP 28; IAIS 2004a). In the context of avoiding abuse of insurance, this could be extended to the investor-to-insurer link.

**Direction of the communication process**

There is often an information asymmetry to be recognized and addressed. For example, communications in the insurer-to-policyholder link have very different obligations and supporting assumptions than communications in the policyholder-to-insurer link. As a consequence, there are linkages to consider from each sender to each receiver of information. Some linkages are high profile and important, as reflected in the existence of laws and regulations governing them. Others are either less important or less formally governed.
MULTIPLE "STRANDS" FOR EACH STAKEHOLDER

Each of the stakeholders identified may have a number of strands or subcategories, each with its own particular set of characteristics. For example,

- **Supervisor.** The supervisory system in a jurisdiction may include a number of supervisory authorities, each with separate roles. The communications between these authorities needs to be considered as well as the communications between the supervisory authorities and entities supervised.

- **Insurer.** There may be different types and scales of insurers to consider, including multinationals (issues around subsidiaries as opposed to branches), captives, composites, and so on. In the insurer-to-insurer link, the potentially different interests of management and employees would be picked up, as would issues relating to the internal workings of corporate governance and the relationships between the management and the board or other governing body of the entity. The insurer-to-policyholder link would cover issues such as the content of annual (or more frequent) statements and other policyholder communications as well as the management of sales and servicing of consumer needs and policies.

- **Investors.** Investors include shareholders in listed entities, shareholders in private entities, participating policyholders in mutual entities, and potential shareholders and policyholders.

- **Intermediaries.** There are different types of intermediaries. Perhaps the major distinction is between brokers and agents, reflecting to whom the intermediary’s primary duty is owed, although many variations exist. See IAIS (1999) for a set of principles expected in the good management of the insurer-to-policyholder and intermediary-to-policyholder links.

- **Policyholders.** This category may cover current, past, and future policyholders. In particular, in some jurisdictions, one issue is the creation of reasonable expectations on the part of policyholders in a sales context and the management of these expectations in an ongoing service context. Generally, from the sales perspective, this includes the issue of appropriate sales illustrations. See ICP 25.

- **Professional infrastructure.** This includes the roles, professional independence, and responsibilities of professional groups such as actuaries, accountants, auditors, and the like, including any standard-setting functions they may have. The need for infrastructure to support such objective professionals is critical to the long-term successful development of the insurance industry (see ICP 1).

- **Market.** There are different aspects of the “market” to consider. These might include the roles of rating agencies; the roles and rules of bourses in listing entities; the roles, influence, and governance of market analysts; the role of the media; and so on. However, policyholders (current and future) are excluded from this reference to “market.”
- **Industry.** This reflects not only direct linkages between insurers and the supervisory authority, but also linkages between the authority and industry associations and other (representative) groups. Liaison with industry and the receipt of constructive feedback from industry are important aspects of a successful supervisory approach. Industry-to-industry links cover issues around competition and collusion and the sharing of information for the prevention of fraud (see ICP 27).

- **Public.** This includes the public as individuals and as represented by various consumer and other special-interest groups, including researchers and academics. Although a supervisor is unlikely to “slant” requirements for the particular interests of researchers and academics, data regarding insurers are of interest to them.

- **Government.** Generally, high-level policy is set by government or by a department of government. Responsibility for ensuring implementation of this policy is given to various government agencies, such as insurance supervisory authorities and regulators of general business activities, including aspects involving share trades and tax collection. It is in the interest of supervisors and those they supervise for there to be clear and open lines of communication. The optimal situation is for the supervisory authority to have and maintain a real independence from the government (see ICP 3). A second aspect might be other government agencies or departments, such as the tax office.

- **Supra-national agencies.** There are valuable linkages to be had with agencies like the IAIS, the World Bank, other regional development authorities, the IASB (International Accounting Standards Board), and similar organizations, especially those that drive international standard setting. These linkages may be direct or via other government bodies.

### Reasonable expectations

The issue of what the recipient of information can reasonably expect from the provider of the information needs to be addressed. This can be a lively and evolving debate that depends on the extent of information asymmetry between the provider and recipient. One established example is the evolution of the concept of reasonable expectations on the part of policyholders. However, the question extends, in principle, more broadly to each pairing of sender and receivers.

### Exercise

4. The introductory section of this module identifies a number of other ICPs in which disclosure plays an important role. Identify the cell or cells of the stakeholder matrix (figure 1) in which these ICPs should be placed.
C. Role of disclosure

This section discusses the role of disclosure in maintaining market stability and enabling stakeholder decisionmaking, considers the special aspects of insurance that influence the need for disclosure, weighs the costs of disclosure against the benefits, and discusses the contributions of other stakeholders to the disclosure process.

Maintenance of market stability

As indicated in section A, disclosure and transparency of information are coming to be accepted as key pillars of financial sector supervisory systems.

For markets to operate efficiently, and with increased stability, stakeholders need to have access to relevant and reliable information about the markets, products offered, and prospective providers in a timely and unbiased manner. Regular and timely disclosure should reduce the volatility of markets and discourage stakeholders from overreacting to change and potentially being arbitraged against. Supervisors concerned with maintaining efficient, fair, and stable insurance markets need to promote and ensure adequate disclosure. As discussed, there is a wide variety of stakeholders whose needs require consideration. Generally, the primary focus of the insurance supervisory authority is on protecting the interests of current and future policyholders. However, other stakeholders also contribute to market efficiency and stability, which assists in protecting the long-term interests of policyholders.

The information needs of the market, and other stakeholders, extend beyond financial and accounting information, such as annual financial statements, to include nonfinancial information, such as reporting on corporate governance, business objectives, and other corporate responsibilities.

Supervisors should recognize that, while they may determine conditions and criteria for disclosure, other stakeholders may legitimately do so as well. An example of this are stock exchanges, which set rules for listing that include disclosure requirements, and rating agencies, which rate companies according to established criteria. While such ratings are not determined from a supervisory perspective and are not part of the supervisory process, supervisors generally maintain a strong interest in the ratings and in changes in them.

With the increasing internationalism of the insurance industry, expectations from other jurisdictions will likely affect a supervisor’s own jurisdiction. As a result, some convergence in the definition of what is appropriate disclosure should be encouraged and anticipated. Supervisory authorities also have an ongoing role to play in establishing expected levels of disclosure and managing their change over time. What constitutes reasonable expectations varies over time, by jurisdiction, and by sector of the financial services industry. However, some principles and objectives are common to all elements of the financial services industry, including insurance, suggesting that there is value in
understanding how others approach the issues (see APRA 2003; Joint Forum 2004). This variation provides insurance supervisors with the opportunity to manage (changing) expectations of stakeholders within their jurisdiction as well as to gain insight into potential future approaches.

Disclosure is of increasing direct importance as a driver of good governance for financial services institutions. A key role for supervisors is to ensure that information disclosed to the various stakeholders is accurate, complete, and appropriate. This objective may be addressed directly by the supervisory authority or indirectly (for example, by mandating independently audited annual financial statements and independent actuarial assessments). A key corollary is to penalize inappropriate or incomplete disclosure of information. This increased reliance on market forces presumes the existence of an effective and efficient market and the presence of effective legal, professional, and governance systems and controls. While this may not always be the case, better disclosure can make developing markets more efficient (IAIS 1997).

The supervisory objective of supporting market monitoring and disclosure, as opposed to assessing the capacity and future prospects of the industry, can potentially be achieved in a relatively short period of time in many jurisdictions. There is value in separating questions regarding the level of sophistication of the industry in terms of products and technical aspects from questions regarding the level of sophistication of the disclosure the industry makes. It is clearly possible to improve the quality and integrity of disclosure on a subject without changing the underlying subject itself. Of course, in the process of enhancing disclosure practices, the subject of the disclosure itself may improve, so a consequence of the disclosure may be that the subject becomes better managed or better understood.

In summary, it is clear that appropriate disclosure is necessary to the long-term stability and prosperity of the insurance industry, the protection of the interests of current and future policyholders, as well as the protection of the interests of other stakeholders. Although necessary, this condition alone does not ensure long-term success.

Supporting stakeholder decisionmaking

The need for disclosure has been addressed at the macro level. In addition, specific issues increase the importance and relevance of disclosure in an insurance context.

There is general consensus that competition alone does not provide adequate incentive for financial services providers, including insurers, to disclose sufficient information on products and other matters. In fact, certain types of competition may discourage full and meaningful disclosure, as there may be an incentive to report only the positive aspects of a product or an insurer in order to gain advantage. Based on this experience, supervisory authorities mandate requirements for the disclosure of information to relevant stakeholders. That is, it is not realistic to assume that all stakeholders involved in a business environment will always have altruistic motives when addressing
their disclosure obligations. Given this, supervisors also need to consider the potential consequences for stakeholders of a failure to disclose information and be prepared to take action against those who do not disclose information as and when required. However, disclosure, of itself, is not adequate to prevent abuse or to ensure that policyholders (current and future) will take responsibility for their own decisions.

The underlying objective of disclosure is to put recipients of the information disclosed into a position to make well-informed decisions. The transparency of the information provided is critical to assisting the stakeholder in making these decisions. Even if they want to, stakeholders simply might not have the knowledge needed to make the best or even a good decision. This inherent information asymmetry is not uncommon in the context of the selling of insurance policies. In such cases, the role of disclosure needs to be considered carefully and monitored. The supervisory authority may undertake this monitoring either directly or indirectly by requiring adequate processes to be in place and then reviewing them periodically. Additionally, disclosure is inherently a passive process. That is, disclosure can ensure that certain information is provided to recipients, but it cannot ensure that the recipients will take any notice of the information provided. Put differently, disclosure is a necessary, but not a sufficient, condition for good decisionmaking by stakeholders. A precondition for good decisionmaking is that stakeholders start with an adequate base of knowledge.

The argument that full disclosure provides adequate protection to the receiving stakeholders is often made. This is particularly so in the context of policyholders, both current and future. However, for disclosure to be considered adequate, the information provided must be accessible. The disclosure of information that is not reasonably accessible (even if complete) is not useful and may even be misleading. Minimum standards need to be applied, and hence specified, for disclosure practices. Further consideration, especially in an ongoing context as opposed to a sales context, should be given to whether, even if information is disclosed, the policyholder can take any constructive action. An example of this might be the purchase of a participating life insurance policy, when, at some time in the future, the bonus attribution process is flawed or abused. Another example might be the impact on the insurance industry of seemingly ever-increasing claims due to asbestos-related events.

The “full disclosure” suggestion also raises the related but separate issue of the need for stakeholder education. This is of particular concern for certain current and future policyholders and may also be for other stakeholders, although the level of education that can reasonably be presumed will depend on the stakeholder. For example, sophisticated investors can legitimately be presumed to understand the investment risks being taken and so the consequences of their actions. In general, the establishment of disclosure requirements does not imply a supervisory obligation to provide stakeholder education, although some supervisory authorities do have this as part of their mandate (see the module on ICP 2 dealing with supervisory objectives). However, this does not prevent supervisors from providing needed background and educational information (for example, via websites), should they choose to do so.
Experience suggests that companies with good overall business practices often practice good disclosure. Consequently, if a provider does not wish to meet good disclosure standards, the supervisor will want to know why. That is, poor practices or contravention of requirements may, to some extent, indicate the need to investigate further.

Some supervisory authorities consider themselves to be primarily “disclosure based”; their objective is to protect stakeholders, to the extent that they need protection, by empowering them to make good decisions based on appropriate information required by regulatory action. This is quite different from a supervisory authority that seeks to protect stakeholders directly from the consequences of their own unwise decisions.

An example of a supervisory authority that considers itself to be primarily disclosure based is the Australian Securities and Investment Commission (ASIC). In the context of insurance products, ASIC’s approach is essentially as follows:

- **Prevention through disclosure.** The goal is primarily to ensure that insurers provide current and future policyholders with adequate relevant information. This is often satisfied by established codes of conduct or codes of practice, with varying degrees of statutory backing, which are monitored and enforced. Such an approach can be effective even in markets that are not considered to be efficient or competitive. This is of particular importance regarding investment products, which typically involve relatively large sums of money and extend over very long time frames. In Australia, a compulsory superannuation (retirement savings) regime is in place under which life insurers may offer investment products that have no insurance component. Life insurers often offer products with a significant savings element through traditional whole-of-life and endowment products.

- **Cure through enforcement.** Unfortunately, abuses of regulations and misconduct will occur. This means that supervisory authorities need to have in place adequate mechanisms both to redress stakeholders who have legitimate complaints and to discipline and punish appropriately those who have abused the disclosure process. An important aspect of the enforcement process is that it is publicly disclosed, providing both a deterrent effect and, potentially, some public education benefit.

While this approach is often discussed in terms of intermediaries and sales practices, the processes are equally applicable in other areas, such as corporate governance and the management of conflicts of interest.

A key aspect of disclosure, no matter in what context or to which stakeholder, is that the information provided should, in general, be in writing. In an environment where electronic information is legally accepted, printouts of e-mails and downloads from the Web are usually acceptable.
This section provides justification for the need for disclosure by insurers in the face of the contention that “most policyholders are either uninterested in the information or unable to understand it.” As noted, a disclosure process is passive and does not necessarily drive actions by the recipients of information. However, without disclosure, stakeholders—prospective or current policyholders in this instance—are unlikely to be able make informed choices, so disclosure is a necessary initial step in the development of an appropriate relationship between the provider and the user of an insurance product. The question of whether (current or future) policyholders are interested in the information is distinct from whether the information is available to them.

Likewise, the question of whether they understand the information, which depends to an extent on regulation intended to ensure that the information is appropriate for the audience, also depends on the level of responsibility each policyholder is prepared to take in the process of purchasing or maintaining a policy. The risk of overdisclosure should also be considered, because too much detailed information can obscure the main message and impede decisionmaking. The management of these issues is addressed in ICP 24 and ICP 25.

Supervisors can support disclosure by publishing information about nondisclosure and complaints from policyholders and by taking action to prevent such events from recurring.

In summary, disclosure is a necessary, but not a sufficient, condition for good stakeholder decisionmaking. A precondition for good decisionmaking is that stakeholders start from an adequate base of knowledge. Disclosure is an inherently passive process, and so the proposal that a “full disclosure” regime provides adequate stakeholder protection, even in the absence of the information asymmetries inherent in insurance, is not supported. To make a disclosure process work, appropriate complaint resolution and enforcement processes need to be available and used by the supervisory authority.

**Special aspects of insurance**

It is widely believed that financial services—and insurance in particular—need to undertake better disclosure than other companies or entities. Insurers and intermediaries have a fiduciary duty, when dealing with stakeholders, to undertake appropriate disclosure, ensure transparency, and provide complete information. This reflects the complexity of the products and their long-term nature as well as the information and knowledge asymmetry inherent in the provision of insurance services.

- **Inherent uncertainty.** The statistical nature of insurance means that uncertainty is inherent in its management—in particular, in the estimation of liabilities. This is particularly important given the long-term and uncertain nature of many insurance covers.
- **Long-term contingencies.** Often the contingencies insured against are very long term in nature—for example, a young person taking out death coverage may have a life expectancy of more than 50 years, claims may emerge for asbestos exposure that occurred up to 50 years ago, savings for retirement purposes may span more than 50 years, and the annuity payouts may extend several more decades.

- **No “rerun.”** In many situations, if the coverage is not honored when claimed, the policyholder has little or no opportunity to recover the loss by starting another coverage contract. The clearest example of this is a death claim. Loss of funds accumulated for retirement purposes would be equally devastating.

- **Large scale.** The sums payable to policyholders on termination or claim typically are large relative to their financial resources. Generally, therefore, policyholders are unlikely to be able to recover from the failure of the insurer to meet its obligations.

- **Atypical nature of insurance contracts.** Insurance contracts are the opposite in some respects of common contracts in that the policyholder often pays premiums immediately, and perhaps also at predefined future times, in return for a future benefit that may be uncertain in both size and time of receipt. While the payments are real and tangible to the policyholder, the benefits can seem abstract and intangible. Further, in many instances, the benefits are triggered by unpleasant and stressful events and are often not paid to the policyholder, but rather to one or more beneficiaries.

- **“Custodial” management.** Management of insurers has a custodial role to play in looking after the interests of policyholders over a long time frame. The duration of the obligations to the policyholders typically greatly exceeds the average tenure of current management, and so care needs to be taken to ensure that these long-term interests are both protected and seen to be protected. Public disclosure by an insurer of its business policies helps to demonstrate this commitment. To varying extents, the primacy of the policyholders’ interests over the interests of all other stakeholders is accepted and in some cases specifically entrenched in law. An example of this is section 32 of the Australian Life Insurance Act of 1995. Managers of other types of companies typically do not encounter such issues.

- **Impact on third parties.** In some cases, the beneficiaries of insurance policies may not own the policies. Disclosure can help to ensure that consequential impacts on third parties are acceptable and appropriate.

In summary, there is a need for more intensive disclosure in the insurance industry than in many other industries for a number of reasons: there is inherent uncertainty due to the statistical nature of insurance covers, the contracts are often very long term and there is no recourse in case of failure, insurance contracts often involve large amounts of money from the perspective of the policyholders, insurance contracts are atypical
and abstract, and management needs to take a long-term custodial perspective in their management of insurers.

**Costs and benefits of disclosure**

Since disclosure requires some effort and resources, it results in additional costs. An important question that needs to be addressed is whether the benefits of the disclosure exceed the costs. Objective assessment of costs and benefits is not necessarily straightforward. There are direct and financially quantifiable costs and potential benefits, but there are also indirect costs and benefits to be considered. Financial analysis may need to be augmented by nonfinancial considerations, both by supervisors and by other stakeholders.

The underlying purpose of disclosure is to provide information so that stakeholders can make balanced and informed decisions. Consequently, when the costs of disclosure are discussed, there is a need to consider not only the direct costs of the disclosure process itself but also the potential costs that might arise should the disclosure not take place. In extreme cases, the cost of nondisclosure can be the failure of the entity and stress in the industry as a whole. While such events may be uncommon, they can be very large in magnitude. In this context, it is perhaps useful to think of the costs of disclosure as analogous to an insurance premium, and a decision needs to be made as to whether the premium provides protection at a reasonable price against the risks inherent in nondisclosure.

Disclosure requirements, if pertinent and properly crafted, should not impose a significant burden on an insurer. If the information is relevant to management, and perhaps also to prudential or financial reporting to a supervisory authority, then it is hard to see why the required public disclosure should create significant incremental costs. In principle, provided the supervisory authority believes there is good cause to request information of insurers, and the request is well crafted, then cost should not be a bar to its provision. In this context, the authority should be prepared to justify the need to disclose the information. Constructive discussion with industry representatives may improve the specification of the information required. However, supervisory authorities may have legal authority to make the final decision regarding disclosure requirements. In such situations, once the decision is made, it is incumbent on industry to abide by it.

It may, perhaps, be argued that certain information is proprietary or commercially sensitive. This may include details about policyholders in which privacy concerns are involved, information about specific products or systems, or detailed data on product lines. Supervisors should either be satisfied that the information to be disclosed is not really commercially sensitive or modify the disclosure requirements appropriately—for example, by providing for its disclosure in aggregated form. While genuine commercial sensitivity may be a valid concern, care needs to be taken to ensure that this concern
does not provide an excuse for nondisclosure and inaction. The stakeholders’ interests in the information need to be considered at the same time.

Responsibilities for governance and risk management are not directly financial matters. While there is a cost to industry in disclosing governance and risk management practices, the effort required to meet those requirements is part of the necessary and appropriate management cost of being in a fiduciary business.

Supervisory authorities need to be prepared to justify the additional costs and effort required to disclose further information and to specify the benefits expected to accrue from this disclosure. This implies the need for a process within the supervisory authority to perform this analysis.

For example, the Financial Services Authority (FSA) in the United Kingdom is mandated to consider whether the benefits of its requirements are proportionate to their burden. This implies an obligation to perform cost-benefit analyses. (See the FSA website, www.fsa.gov.uk.)

In summary, the costs and benefits of disclosure should be assessed, and disclosure should be required if the benefits outweigh the costs. In practice, the assessment of both costs and benefits can be difficult, and subjective views may be involved. A starting point may be that well-crafted and pertinent disclosure of information, relevant to the internal management, should be expected to have low incremental costs to insurers.

**Role of the supervisory authority in promoting disclosure**

As a core part of its role, the regulatory authority sets standards that supervised entities must meet. Inherent in the nature of regulation, such standards are generally minimum standards applicable to all those being supervised. It is incumbent on those being supervised to decide how much higher their internal standards for the management of their business should be than such minimum requirements. Not all members of a group will be able to attain “best practice,” which, after all, is fundamentally a comparative assessment. The only logical exception to this is if the intent is to have each member of the group attain the same level of practice, which implies that no member is better, or worse, than any other member. Such an aspiration is potentially both limiting and counterproductive in any environment in which innovation and improvement are sought. The supervisory focus should be on determining and enforcing what is acceptable practice, encouraging the development of better practices, and raising the bar as better practices emerge.

Essential criterion d requires the supervisory authority to monitor the information disclosed by insurers and to ensure compliance with disclosure requirements. This responsibility is discussed in section D of the module.

In the context of improving disclosure practices, the supervisory authority should have ongoing discussions with industry and industry organizations. While industry participation can enhance the regulatory process by improving understanding and hence
“buy-in,” supervisors need to be aware of the risk that industry may be slow in coming to agreement about or accepting the need for change. Consequently, the supervisory authority must be prepared to impose disclosure requirements, where necessary, even in the face of industry disagreement.

Additionally, the supervisory authority has an important obligation to ensure that the marketplace is aware of its initiatives and standards in the many areas it influences. That is, the supervisory authority’s disclosure of its own practices, expectations, and enforcement to the market is a critical part of the supervisory process, as it is able to “lead by example” and enforce its requirements more credibly.

The need for disclosure by the supervisory authority is noted at various places in the ICPs, including the following:

- **Introduction, paragraph 10.** “The supervisor must recognize that transparency and accountability in all its functions contribute to its legitimacy and credibility and the efficiency and stability of the market. A critical element of transparency is for supervisors to provide the opportunity for meaningful public consultation on the development of supervisory policies and in the establishment of new and amended rules and regulations. To further ensure the proper and efficient operation of the market, supervisors should establish clear timelines for public consultation and action, where appropriate.”

- **ICP 1, Conditions for effective insurance supervision, essential criterion d:** “Accounting, actuarial, and auditing standards are comprehensive, documented, transparent, and consistent with international standards. Accounting and actuarial standards are applied and disclosed in a manner that allows current and prospective policyholders, investors, intermediaries, creditors, and supervisors to properly evaluate the financial condition of insurers.”

- **ICP 2, Supervisory objectives, essential criterion c:** “In the event that the law mandates or specifies multiple objectives for insurance supervision, the supervisory authority discloses and explains how each objective will be applied.”

- **ICP 2, Supervisory objectives, essential criterion d:** “The supervisory authority gives reasons for and explains any discrepancies from its objectives.”

- **ICP 3, Supervisory authority, essential criterion j:** “The supervisory authority has transparent processes and procedures for making supervisory decisions. Supervisory decisions are demonstrably consistent.”

- **ICP 3, Supervisory authority, essential criterion k:** “All material changes to the insurance legislation and supervisory practices are normally subject to prior consultations with market participants.”

- **ICP 3, Supervisory authority, advanced criterion l:** “Representatives of the supervisory authority publicly explain their policy objectives and report on their activities and performance in pursuing their objectives.”

- **ICP 4, Supervisory process, essential criterion a:** “The supervisory authority adopts clear, transparent, and consistent regulatory and supervisory processes.
The rules and procedures of the supervisory authority are published and updated regularly.

- **ICP 4, Supervisory process, essential criterion d:** “The supervisory authority makes information on its role publicly available.”
- **ICP 4, Supervisory process, essential criterion g:** “The supervisory authority publishes a regular report—at least annually and in a timely manner—on the conduct of its policy, explaining its objectives and describing its performance in pursuing its objectives.”
- **ICP 4, Supervisory process, advanced criterion h:** “The supervisory authority provides and publishes information about the financial situation of the insurance industry and observations on major developments in the insurance or financial market.”

The supervisory authority’s disclosure and enforcement of expected practices are of great importance in corporate governance, prudential requirements, and dealings with consumers.

**Influence of other stakeholders**

Supervisors work in an environment that is complex and influenced by many stakeholders. In their role of promoting safe, efficient, and fair insurance markets, supervisors need to be aware of these other influences and expertise. Where possible, without compromising their primary role and responsibilities, supervisory authorities should work cooperatively with these other stakeholders. In most cases, either other stakeholders do not have a formal supervisory role or, if they do, there are differences between their objectives and those of the insurance supervisory authority. However, the supervisor should be aware of information disclosed, both formally and informally, in response to the needs and requirements of other stakeholders, examine it for consistency with information provided to the supervisory authority, and seek to avoid conflicting requirements, where practical.

Other stakeholders also may influence disclosure:

- Stock exchanges, which have a set of requirements to support the listing and disclosure to the investing public
- Rating agencies
- Accounting, actuarial, and other professional standard setters (both national and international)
- Corporation law
- Other supervisory and related authorities, including authorities responsible for taxation, anti-money laundering, and so on, such as police and other enforcement agencies; where financial services and insurance supervision are not car-
ried out through a single integrated authority, good interagency communication and information sharing are important

- International initiatives and agencies—for example, the World Trade Organization.

Following a number of large corporate (including some insurer) failures, a lot of effort has gone into developing disclosure requirements for corporate entities and, in particular, for companies listed on stock exchanges. Much of the work has focused on corporate governance and risk management, with considerable emphasis on the role of auditors and other professionals following the collapse of Arthur Andersen. The International Financial Reporting Standards, which are being adopted in many jurisdictions, include specific disclosure requirements for insurance.

The Australian Stock Exchange (ASX) has listed on its website, www.asx.com.au, the criteria that apply to listed entities, including insurers (see, in particular, the “market supervision and rules” section). Principle 5 of the 10 principles of good corporate governance is “make timely and balanced disclosure” (ASX 2003). Guidance is provided on how this aim may be achieved.

**Exercise**

5. A senior executive of an insurer in your jurisdiction has called to protest that your requirement that a risk management plan be submitted within the next three months is unreasonable, as it will cost too much to produce. How do you respond? If the executive has made a good case due to the complexity of the requirements, how far would you be willing to compromise and why?
D. Disclosure in practice

This section discusses practical aspects of disclosure, beginning with criteria that can be used to assess the usefulness of particular disclosures. The information that might be disclosed is considered, including audited financial statements, risk management practices, the use of reinsurance, and investment risks. The types of information of particular interest to policyholders and investors are discussed. The contributions that a supervisory authority’s own disclosures can make are considered, along with the information channels that can be used by both insurers and authorities. Finally, corrective measures that might be taken by a supervisory authority to deal with disclosure inadequacies are discussed.

Assessing the usefulness of disclosure

Several criteria are available to assess the usefulness of publicly disclosed information (see IAIS 2002). These criteria can also provide a starting point for assessing the usefulness of information provided to the supervisory authority on a confidential basis. The criteria should be applied at a level that is reasonable and appropriate, consistent with the importance of the matter under discussion.

Information disclosed should meet the following criteria:

- **Relevant.** Relevance is assessed in terms of its significance to the user. If there is a substantial likelihood that the user would consider information to be important in making a key decision, then it is likely to be significant. It follows that insignificant information is not generally required to be disclosed. Given that there are many different users, supervisory guidance in determining relevance may be appropriate.

- **Reliable.** Information should fairly represent that which it purports to represent. In particular, as far as practicable, information should represent the economic substance of events and transactions as well as their legal form, with the economic form prevailing if an inconsistency arises. Reliability also implies that information is verifiable to a reasonable extent, is unbiased, is objective, and has no material omissions.

- **Timely.** The information is provided with sufficient timeliness and in sufficient frequency to give a current and meaningful picture of the issue in question, while retaining appropriate reliability. In unusual circumstances, this may mean that entities need to report more frequently than would otherwise be required. The supervisory authority may provide guidance on the circumstances under which such reporting would be necessary.

- **Accessible.** The information should be disseminated in a way or ways designed to allow it to be understood by its intended audience.
• **Comprehensive.** The information presented should be complete and enable the user to form a balanced view on the matter under discussion. For example, it should permit an assessment of relevant risks and their management, including sufficient detail to permit assessment of the impact of each important issue relating to these risks.

• **Comparable among insurers.** Where appropriate, information should be prepared in accord with applicable and accepted professional standards. Where such standards are available, compliance with them should be stated explicitly and any noncompliance explained and justified. The use of material judgments in the process should be identified. Whether standard processes are used or not, a description of the data used, assumptions made, methodology used, and validation process should be provided.

• **Consistent over time.** Methods, assumptions, and data analyses should be consistent over time. Where changes are made, the changes, their basis, and their impact should be disclosed. This facilitates the development of realistic trends over time.

The criteria outlined above are all reflected in essential criterion a. The following criteria could also be considered:

• **Assessment of uncertainty.** In many cases in insurance, such as the projection of long-term liabilities, there is inherent uncertainty in the results obtained. Where there is possible uncertainty inherent in methodologies, assumptions, or data used, this uncertainty should be assessed. If the inherent uncertainty is considered likely to be significant, it should be described appropriately and explicitly. Expectations as to the relative reliability of such results need to be managed appropriately and explicitly. Following from the reliability criteria given above, this may be a context in which some form of expert review or independent audit may be relevant (see also IAIS 2004c regarding sources of uncertainty).

• **Verification.** A characteristic of reliability is that the information is verifiable. This is a passive perspective. Supervisors should take an active approach to verifying the information provided, both to them directly and to other stakeholders. The verification may be direct or indirect through third parties. In this context, the role and reliability of expert analysis and independent audit may be relevant. Decisions regarding the extent of the verification should consider the significance of the information. The supervisory authority should also have the capacity to require further independent analysis should this be deemed appropriate.

• **Appropriateness.** In some cases, depending on the purpose, timing, and the audience, consideration should be given to whether disclosure is in the interests of all affected stakeholders. That is, there is little value in simply having disclosure for the sake of disclosure. In the context of insurance where there are inherent and ongoing information asymmetries, disclosure of information can be
counterproductive, especially in the context of disclosure regarding prudential matters. For example, requiring the disclosure of detailed results of stress tests may raise concerns that the insurer and the supervisory authority would have difficulty addressing (see APRA 2004).

- **Balance.** The balance of information disclosed also is important and is related to the requirement that the disclosure be “comprehensive.” That is, the disclosure of biased or incomplete information can increase the likelihood that users will misinterpret the information or be led to erroneous conclusions. While the information disclosed may be correct as far as it goes, the omission of relevant information can lead to an unbalanced perspective. The typical user generally cannot assess or know what is not disclosed, because such an assessment generally requires expert knowledge to identify the missing components, let alone understand their magnitude.

In making assessments against these criteria, some underlying presumptions about the characteristics of the provider of information and the assessor should be recognized. The assessment of these criteria may vary, depending on which market or type of stakeholder is receiving the information.

- **Reasonably qualified.** The person or entity making the assessment of the disclosed information should be reasonably qualified and experienced to do so. The disclosure regime does not have a direct role in addressing user education, although the discloser of information may, separately, determine the need for user education and take an appropriate course of action. For example, it may not be reasonable to expect policyholders in general to understand some of the information provided. In such circumstances, it may make sense to expect them to obtain appropriate third-party assistance to fulfill the criterion of being reasonably qualified.

  This emphasizes the requirement of accessibility. The audience for which information is intended has a major impact on what information is needed and how it should be presented. In particular, to be relevant to varying audiences, the same information will likely need to be presented in different formats at different levels of detail.

- **Reasonable attempt.** The person (or entity) making the assessment should make a reasonable attempt to understand the information presented and to put the information into context, from both the entity and industry perspectives. This includes a reasonable recognition of the practical constraints under which the disclosers of information and their supervisors operate.

- **Provider intent.** The provider of the information should prepare the information with appropriate care, diligence, and intention to facilitate the proper objectives of the disclosure. Accordingly, the supervisor needs to understand the environ-
ment in which the information was prepared, such as the processes used and their quality.

Another way of viewing this is that it is important for the supervisor to gain insight and to assess the quantitative as well as the qualitative aspects of the information disclosed. This includes understanding the causes and drivers of changes or movement in results as well as reporting such changes. In cases where there may be an intent to mislead, the methods used may nevertheless be acceptable. The results provided might not be wrong, but they might be inappropriate, as they are not provided in the spirit of the disclosure requirements. For example, the discloser might not point out that illustrated dividends are not guaranteed. The supervisor has a responsibility to assess the validity of disclosed information from the perspective of its intent, as well as have the appropriate powers and processes to pursue subsequent investigations. A specific example of this is when fraudulent results are suspected.

See also IAIS (1999), which, although focused on the retail insurance environment, outlines principles that clearly emphasize the need for the appropriate behaviors and attitudes to be embedded in the operation of an insurance business.

The insurance supervisory authority has two distinct roles to play in the context of disclosure: supervising the public disclosure of others and making its own public disclosures. The supervisory authority may control certain aspects of public disclosure by insurers or other stakeholders in the insurance industry. In these cases, it needs to assess and police the adequacy of the disclosures used. However, other authorities may control different aspects of disclosure, in which case liaison with such authorities would be valuable to both the industry and the insurance supervisor.

In fulfilling its supervisory mandate, the authority should apply these disclosure criteria to its own actions. This is a “practice what you preach” type of test. In some cases, where the supervisory authority does not have the legal power to require the industry to disclose certain types of information, it may have the legal power to disclose such information itself. The supervisory authority has a potentially important role to play here, as it can collect, collate, and analyze information across the industry it supervises.

**Information to be disclosed**

In the context of disclosure of public information, the supervisory authority needs to address the following areas, at a minimum: business activities; financial position; financial performance; risk management; bases, methods, and assumptions used to prepare information; and business management and corporate governance (IAIS 2002). In addition, it needs to decide whether to specify the format of such disclosure. In taking on
such a role, the supervisory authority should balance the need for consistency with the need for information to be disclosed in a manner that providers consider appropriate to their circumstances.

**BUSINESS ACTIVITIES**

Business activities include the material lines of business the insurer is currently engaged in or proposes to become engaged in and future business plans for these areas. They should cover not only the insurance and business risks and their management, but also the necessary supporting business activities such as distribution management, information technology development and management, corporate affairs, and so on.

**FINANCIAL POSITION**

Information should be provided regarding the current financial position of the insurer, to permit an assessment of its ability to meet its current obligations to policyholders and to provide a return on investment to stakeholders, including participating policyholders. Relevant information includes descriptions of assets, liabilities, capital, and risks.

**Assets** should include a categorization of assets held by generally accepted asset categories, an assessment of counterparty risk, the bases on which assets are valued, the impact of the use (if any) of derivatives, liquidity, and changes in investment structure since the prior reporting date. In an insurance context, the information should assist the user in determining whether the types of assets chosen are consistent with the nature of the liabilities taken on by the insurer.

**Liabilities** should include information on the nature and timing of liabilities or technical provisions and, in particular, the degree of uncertainty in the estimation of future liabilities (for example, the provisions that have been made for adverse deviations in experience). The impact of reinsurance should also be included; that is, results gross and net of reinsurance need to be provided. This is particularly relevant when small, specialist, or financially unsound reinsurers are used, as the potential for failure may be higher than is the case for the major international reinsurers. The segmentation of liabilities by major accepted product lines should also be expected.

**Capital**, including the amount of regulatory capital available, should be disclosed. If applicable, it could be noted whether the capital is below one of the regulatory control levels. The assets supporting regulatory capital requirements also need to be detailed, so the quality of capital provided can be assessed.

**Risks**, including a realistic assessment of the risks, and their interactions, faced by the insurer, should be provided. Ultimately, the insurance business is about managing risk, so it is inappropriate to expect that risk can be eliminated no matter how much capital is held.
FINANCIAL PERFORMANCE

Information about an insurer’s current financial position is, of itself, inadequate to allow the market to form a view on the insurer’s ability to meet future obligations. Meeting future obligations depends on future performance. While past history cannot predict future results, in a stable environment with established management structures and strategies, historical experience may provide a useful basis from which to develop future expectations. Topics that assist in the development of expectations around future results include (a) analysis of historic profit sources, including an explicit analysis of the sources of historic profits and losses and the recognition of geographic impacts, reinsurance, underwriting and claims management, and other influences on performance, and (b) segmentation by major product line, including an investigation of results by each product line, as well as in aggregate, because insurance risks may be correlated to varying degrees.

RISK MANAGEMENT

Disclosure of an insurer’s assessment of its risk exposures and strategies for managing and mitigating the risks identified is critical to assessing an insurer’s ongoing stability and viability. This involves an explicit assessment of the risk appetite of the board of the insurer and the steps it has taken to ensure that returns are consistent with the risk profile it has adopted. Insurers face many risks, and it is important to recognize that these risks may not be independent of each other. Consequently, an insurer’s risk management policy becomes a matter of great importance.

BASES, METHODS, AND ASSUMPTIONS USED TO PREPARE INFORMATION

For public disclosure to be effective and accepted, the methodologies used to derive results should be disclosed, as well as the results obtained, in sufficient detail so that experts can assess their appropriateness. Methodologies must be consistent across reporting periods in order to see trends.

BUSINESS MANAGEMENT AND CORPORATE GOVERNANCE

Market participants also need information regarding an insurer’s ability to manage itself in the long term. Issues to consider include competitive positioning, corporate governance policies, appropriate structure and policies, management of outsourcing and strategic alliances, and ability to meet supervisory expectations. Competitive positioning is self-evident. Corporate governance policies—the policies and procedures by
which an entity manages itself—should be explicit and available to the supervisor and other stakeholders. For example, the structure, mandates, and membership of board committees should be disclosed. An insurer should have in place adequate policies and procedures to support its need for ongoing public confidence. It should be able to demonstrate its resilience based on these policies. For example, the insurer should disclose its organizational structure. The management of third parties on whom the insurer may be dependent is also critical to the ongoing success of the insurer. While performance of a function may be outsourced, the responsibility to policyholders for these functions cannot be outsourced. Consequently, a key issue for supervisors, when assessing outsourcing arrangements, is to ensure that the supervisory authority has adequate access to information. This, in turn, requires the enforcement of appropriate disclosure of information, either direct from the service provider to the supervisor or from the service provider to the outsourcer and then to the supervisor. Finally, the insurer should disclose the regulatory framework to which it is subject and significant actions it has taken to meet supervisory expectations.

**SUMMARY**

These five areas are all reflected in essential criterion b. Advanced criterion e goes further, requiring disclosed information to include quantitative information on relevant risk exposures.

Different stakeholders have different levels of interest in each of these areas and may take different views on the importance of results reported in each area. The need for disclosure is not static and should be assessed regularly to ensure that the requirements remain appropriate as conditions and products change.

Joint Forum (2004) indicates that, based on a survey of the 2002 annual reports of non-life insurers, “The majority … provide disclosures regarding paid losses [claims] and loss adjustment expense, incurred losses and loss adjustment expense, and loss ratios. However, only a few firms cover pricing adequacy. In addition … most insurers also discuss trends and provide breakdowns of premiums, reserves, and losses.” Suggestions for improved disclosure are made in a number of areas, some of which have been incorporated in IAIS (2004c).

**Audited financial statements**

Essential criterion c requires that insurers produce audited financial statements at least annually and make them available to stakeholders.

Generally, corporation laws and other legal requirements mandate the preparation of audited financial statements. The external audit is important since it should be conducted independently of the insurer and should be performed in accordance with pro-
fessional auditing standards. Although the accounting standards for life and non-life insurance sometimes differ, reflecting the specialized nature of the businesses, auditing standards are the same for each. Also, the role of the external auditor for an insurance company is often subject to supervisory review. In many jurisdictions, an appointed auditor (or a similar professional) has a statutory role, and those performing such a role must meet experience and other criteria to the satisfaction of the supervisory authority.

Audited financial statements are generally included in annual reports, which are often made widely available. For example, many insurers publish their annual report, in full, on their website. In many jurisdictions, insurers are required to send all shareholders a copy of the full annual report, and policyholders can receive copies on request.

The external audit plays an important role in oversight and as an adjunct to corporate governance (in particular, internal audit and compliance). Supervisors generally review the work of auditors with great interest and in some cases choose or, due to lack of resources, may even be forced to rely on the work of external auditors. In such circumstances, supervisors need to consider what assurance they have of the quality and integrity of the external audit processes used and work performed. They also need to recognize that the supervisory role differs from that of the auditors and that supervisory decisionmaking cannot be outsourced to external auditors or other parties.

The major liability of an insurer is generally its technical provisions (claims and other policyholder liabilities). In jurisdictions where there are few or no actuaries, both the development and review of technical provisions can be a difficult matter. It is one thing for auditors to express a view on whether technical provisions have been computed in accordance with specified requirements and another to assess the adequacy of those provisions. (See the ICP 20 on liabilities module.)

Financial statements, whether presented in annual reports or separately, typically contain the following sections (the terminology may vary by jurisdiction):

- The *directors’ report* summarizes the business activities and results for the reporting period, presents declarations, and mentions key issues and events, and their consequences, that occurred during the reporting period. It also offers a view on future issues, risks, and business opportunities.
- The *auditor’s report* provides the opinion of the independent auditors on the financial statements. Where the auditors disagree with the financial statements as presented, they may “qualify” their opinion.
- The *directors’ declaration or statement* certifies that the financial statements are “true and fair” and that there are reasonable grounds to believe the company will be able to pay its debts as they fall due. For insurers, this may include a declaration that solvency requirements have been met continuously.
- The *income statement* summarizes the profit and loss for the reporting period on the basis of accounting used for the financial statements and includes income, expenditures, and tax.
• The statement of changes in equity shows how owners’ equity has changed between the date of the prior balance sheet to the current balance date.
• The balance sheet summarizes the assets, liabilities, and shareholders equity at the balance date (with Assets = Liabilities + Equity). In some jurisdictions, assets and liabilities are split into current and not current, reflecting the expectation that they will be paid, received, or removed in less than 12 months or more than 12 months from the balance date, respectively.
• The cash-flow statement shows the sources and uses of cash during the reporting period. These are usually split into cash flows from operational, investment, and financing activities.
• Notes to the accounts provide additional information on the income statement, balance sheet, and cash-flow statement. In an insurance context, items include topics such as accounting policy, revenue and expenses, tax, equity, assets, dividends, reserves and retained earnings, technical provisions for life insurance, reinsurance arrangements, especially if offshore entities are involved, other liabilities, earnings per share, staff pension and benefit obligations and funds, controlled entities, and contingent liabilities.

See also module 12A for an introduction to insurance accounting.

Risk management

The IAIS has developed some targeted guidance on certain aspects of disclosure for insurers, including IAIS (2004c). (Work is under way on similar standards for life insurance disclosure.) This document makes specific reference to ICP 26, and its key points are summarized as follows:

• Supervisors’ roles. The IAIS standard sets out specific requirements for disclosure to facilitate the assessment of technical performance and risk of insurers and describes the role of the supervisor in enhancing disclosure by insurers.
• Disclosure by significant business class. The standard suggests that “significant” may be a minimum of 5 percent of premiums earned or claims paid. Nonproportional reinsurance treaties are included as a separate class.
• Disclosures of analysis of technical performance. This analysis covers (a) pricing adequacy—loss (claims), expense, combined, and operating ratios, (b) provision adequacy—historical runoff results regarding provisions for incurred losses and provisions for future losses and claims development triangles, (c) claims statistics—statistical information and trends for homogeneous classes of business, (d) risk concentrations—exposures large enough to produce losses that may threaten the insurer’s economic health, including, at a minimum, geographic, economic, sectoral, and reinsurance concentrations, (e) reinsurance and other
risk mitigation—quantitative data supported by qualitative information, and (f) capital—components of regulatory capital by its quality, along with some historical ratios.

- **Disclosure of key assumptions and sources of measurement uncertainty.** This includes the key assumptions and methodologies as well as the level of uncertainty associated with reported results.

- **Disclosure of sensitivity and stress testing and scenario analysis.** This includes the (a) a broad outline of the nature of tests and how the results are used, (b) the minimum set of standardized sensitivity analyses prescribed, if any (impact of minor changes in a single underlying assumption or variable), and (c) the results of sensitivity analyses; the standard does not require disclosure of the results of stress tests.

Understanding how events can affect both the asset and liability sides of a balance sheet, cash flows, and the interplay between assets and liabilities is central to understanding and managing an insurer’s technical performance. The longer the term of the liabilities, the more important these tasks and disclosures become, which may heighten their importance for life insurers. The supervisory authority should consider how the accuracy and reliability of the information disclosed can be assessed and, in cases where it is not suitable or reliable, be able to take appropriate corrective action. This highlights the need for the supervisory authority to have the technical capacity to be able to monitor and assess the information required to be disclosed.

Reinsurance is an important tool that insurers use to manage their risks. The IAIS has developed specific guidance on the disclosure of a particular type of reinsurance—finite reinsurance—by insurers. This is set out in IAIS (2005a).

Recent developments in the area of finite reinsurance, including its improper use, have highlighted the need for supervisory authorities to address this form of reinsurance. For example, authorities are enhancing their information gathering by requiring explicit and more detailed reporting of reinsurance transactions.

ICP 19 discusses the role that reinsurance can play in enhancing the stability of direct insurers.

**Investment risks**

The IAIS has also addressed the disclosure of investment risks and performance in IAIS (2005c). The key points are as follows:

- **Minimum disclosure requirements** should be established on investment risks and performance for insurers and reinsurers; their application in a particular jurisdiction should reflect materiality and other relevant local issues.
• **Investment objectives, policies, and management** encompass (a) qualitative information regarding investment strategy, performance management, instruments used, risk tolerance, stress testing, and outsourcing arrangements; (b) asset-liability management processes and models used; (c) management structure and organization of insurer's investment management function; and (d) where investment objectives, policies, and management differ significantly between parts of the insurer, separate disclosure for each part.

• **Risk exposure** includes information, including quantifiable data, about the insurer’s currency, interest rate, credit, liquidity, and concentration risks.

• **Asset class segregation, description, and profiling** entails (a) grouping assets with similar characteristics or risk into asset classes, (b) disclosing information by asset class, and (c) strongly recommending the disclosure of market value or fair value.

• **Performance measurement** analyzes actual returns on assets and, where relevant, components of such returns.

The underlying objective of such disclosures is to have insurers describe both qualitative and quantitative information to the market regarding investment objectives, policies, and practices to permit the market to form a view on the risk and return behavior to be expected regarding the insurer's asset portfolio. The supervisor should consider how the accuracy and reliability of the information disclosed can be assessed and, in cases where it is not suitable or reliable, be able to take appropriate corrective action. This highlights the need for the supervisory authority to have the technical capacity to monitor and assess the information disclosed.

**Disclosure to policyholders**

Policyholders purchase insurance policies for either protection or investment purposes. Insurance policies can protect against a risk, when the economic consequences of that risk are adverse to the policyholder and the policyholder considers the consequences too large to bear directly. Some types of insurance policies can provide higher or more secure investment returns than the policyholder expects to obtain through direct investing or other investment vehicles.

Life insurance sometimes combines these two basic purposes. Non-life and health insurance only offer insurance coverage. In most cases, the policyholder is transferring risk to the insurer, and so the policyholder’s primary concern is long-term security.

Policyholders and prospective policyholders need access to information that can permit them to assess the insurer’s long-term viability. The question of whether they have the capacity to make that assessment is a different matter. Listed insurers are generally required to make copies of their annual report available to shareholders, and insurers often are required by law to make copies of their annual report available to
policyholders. Annual reports should contain information regarding solvency, future business plans, and the like. With the theoretical exception of participating life insurance policies, where policyholders have an interest in the insurer from the perspective of sharing in annual profits, the policyholder is not usually interested in the insurer itself as an investment.

In the process of accepting (or not) the risks that policyholders seek to insure against, the insurer performs its underwriting process and tests. At this point, both the insurer and prospective policyholders must disclose all material information that can reasonably be expected to be known at the time. This principle of “utmost good faith” (uberrima fides), which is required of both parties, makes insurance contract negotiations significantly different from ordinary commercial contract negotiations. Requiring all parties to reveal all relevant information, the obligation of good faith imposes far higher standards than the standard obligation not to be dishonest and the doctrine of “buyer beware” (caveat emptor). The “buyer beware” doctrine imposes on the buyer the obligation to discover any defect in goods or services purchased.

Further, once an insurance contract is offered to the prospective policyholder, the insurer is legally considered to have exercised its opportunity to make terms and conditions. That is, once the policyholder accepts the insurance contract, the insurer generally loses the opportunity to modify the contract without securing the prior agreement of the policyholder.

In terms of the insurer's dealings with the policyholder, in both the sales and ongoing service contexts, the insurer is obliged to meet all legal and regulatory requirements. These would include, for example, the provision of annual policy statements and other required materials regarding the policy.

In the context of the policyholders' dealings with the insurer, these obligations are generally set out in the policy documents provided as part of the execution of the policy. See ICP 25.

**Disclosure to investors**

Shareholders and other investors, such as bondholders, are interested primarily in the financial performance of the insurer; they seek to achieve a satisfactory return on the capital they have invested. This contrasts with the policyholder's primary interest, which is assurance that the insurer's promises and obligations under the insurance contract are fulfilled in a timely manner. While these interests are not exclusive, they do lead to different perspectives. For mutual insurers, participating policyholders have two distinct roles: as owners of the entity and as policyholders. Life insurance policyholders with participating policies issued by shareholder-owned insurers, while sharing in annual profits according to the terms of their policies, do not have an ownership role.

Investors in an insurer, just as those investing in any other commercial entity, expect that all relevant legal and regulatory obligations will be met. In the context of disclosure,
this includes relevant reporting, such as annual reports and other financial information, as well as appropriate checks and assurances that other appropriate reporting has been completed in accordance with law and standards applicable both generally and specifically to insurers.

**Information channels**

Various information channels can be used to disclose information. The choice of the channel or channels to be used, and the timing of the dissemination of the information, will depend on the type of information, its intended audience, and cost and control issues. In some cases, there may also be legal or regulatory requirements, such as a requirement to send individual policyholders annual statements regarding the position of their policies as of a specific date or to provide the supervisory authority with specified statutory returns in a given time frame.

Where information is intended or required to be made widely available, care needs to be taken to ensure that this is actually the case and that specific subsets of a target audience are not deliberately advantaged over others. Such issues can become difficult to identify and address since in some cases dissemination of information is informal, in other cases establishing unfair advantage is difficult to prove, and the ability of recipients to use information may vary. Such difficulties may arise in the way in which entities choose to brief the market or analysts.

A useful distinction is whether the information channels promote active or passive dissemination. Passive dissemination means that, while the information is made available, it is generally the responsibility of potential users to choose whether or not to obtain it. An example of this is the placement of information on a website. Active dissemination means that information is brought to the user. An example of this is the mailing of annual financial statements to investors and annual policy statements to individual policyholders. In these cases, a policy decision has been made to take reasonable steps to ensure that the recipient receives the information, as opposed to just making the information available. With the evolution of technology, many methods of communication can be used in both active and passive manners. Interactive technologies, such as some websites and telephone systems, can be used for both outward and inward communication.

A number of information channels are available, including the following:

- **Direct communication** may include the traditional means of mail and recent technologies such as call centers and e-mail. These may or may not be personalized. Issues are now arising regarding privacy, the use of outward-bound call centers to solicit sales, the control of spam e-mail, on-line “phishing,” and other potential abuses of technology.
• **The media** include radio, television, and all forms of print media that can serve as intermediary channels between the sender of information and the intended recipients. Also included are press releases, briefings, and the like.

• **Websites** can provide increased opportunities for the provision of information. Usually, they are passive sources of information, but their global accessibility, at all times of the day, makes much more data available than ever before. Section F includes references to the websites of several insurers, as examples of the use of this information channel. Figure 2 provides examples of the types of corporate information disclosed on insurers’ websites. However, it is not always easy to confirm the reliability and authenticity of data available over the Internet, especially where “third parties” (that is, not the insurers or the supervisory authorities) are providing the information.

While digital technology has opened up new opportunities for communication, including for selling and servicing insurance policies, the IAIS has affirmed that the basic principles of insurance supervision—the protection of policyholders and potential policyholders—remain unchanged. The method by which this should be achieved may, of course, change. See IAIS (2004b).

Supervisory websites can be a powerful tool for ensuring that supervisory policy, information, and requirements are continuously up-to-date and publicly available. Further, a free media with access to information can assist the supervisory authority in bringing to light issues of supervisory interest or concern. Supervisors should be aware of media activity and, to the extent practical without compromising (in fact or perception) supervisory obligations, develop links with the media as a channel of communication.

Supervisory authorities should therefore ensure that appropriate policies are in place, for themselves and the entities they supervise, re-
garding use of the available communication tools. As the communication environment is changing rapidly, supervisors need to be flexible and review their policies regularly.

**Corrective measures**

It would be ideal to be in the position where all supervised entities disclosed all required information within specified time frames with appropriate accuracy and commentaries—that is, that all the criteria discussed in this module were fully met. In practice, this is unlikely for a variety of reasons.

Consequently, supervisory authorities need to have an array of tools that they can use to enforce the required disclosures. The appropriate tools will depend on the particular disclosure in question, the circumstances of the entity, the stakeholders addressed, and the supervisory context. For example, a serial offender may be treated differently than an entity missing a deadline by one day and contacting the supervisory authority to indicate this. The enforcement process needs to be managed with care, as the supervisory authority must achieve and retain the respect of the industry and other key stakeholders as being fair, consistent, and appropriately forceful. While this comment is made with respect to disclosure, it is also applicable in the broader context of supervision, and a supervisor’s reputation for integrity and care will usually carry over from one area of supervision to others.

Supervisory tools should be provided for by legislation or regulation, and the supervisory authority should have the capacity and desire to use them, taking legal action if necessary. The following tools are often available:

- **Deterrents and penalties.** These can include monetary fines or other penalties and the removal or restriction of licenses for a period. License controls may be more appropriate for intermediaries than for insurers, except in the most serious cases.

- **Publicity.** The reputation of an insurer and related service providers (including intermediaries) is generally a valuable asset. Publicity indicating noncompliance with supervisory obligations will not enhance a reputation, assuming that the reputation of the supervisor is in good standing. The use of publicity and the media can be an explicit supervisory tool, particularly in the context of consumer protection and the supervision of intermediaries.

- **Supervisory powers.** The supervisor should have an array of powers of increasing severity (see ICP 15 on enforcement or sanctions). These could include, for example, (a) specific directions—instructing entities to produce specified information in a given time frame, with attendant penalties for noncompliance; (b) external experts—having the power to bring in external experts, typically at the entity’s expense, to conduct investigations for the supervisory authority; and (c) direct intervention—intervening because failure to disclose important informa-
tion can be a sign that an entity is in distress. In such cases, the supervisory au-
thority may need to take drastic actions that may, ultimately, lead to the windup
of the entity.

Supervisory authorities also have the potential, directly or indirectly, to play a pre-
ventive role by supporting the education of insurers, intermediaries, and professionals
such as auditors and actuaries on disclosure issues. Licensing and license renewal re-
quirements can reinforce the need for such education.

**Exercises**

6. Outline the key criteria for assessing the usefulness of disclosed information.

7. A financial information service provider is proposing to publish comparative unit prices for unitized (variable) investment products and suggests that this will provide investors with a clear guide to performance and enable them to purchase the most appropriate products. Do you believe that such information will be both appropriate and sufficient to support the investors’ decisionmaking? Explain your reasons.

8. Review the annual reports of several major insurers in your jurisdiction and compare their disclosures with each other and with the items discussed in this section of the module.
E. Summary

This module has discussed the varied needs for and roles of disclosure. Disclosure is a critical pillar of the overall supervisory approach. Timely, reliable, and appropriate disclosure of information to supervisory authorities and other stakeholders is essential for the long-term success of any supervisory regime.

While this module has focused on the market as a receiver of information, the stakeholder matrix in figure 1 demonstrates the many important components in the broader arena of disclosure. The need for disclosure and transparency between all potential sender-receiver pairs of stakeholders, at multiple levels, must be addressed. The entrenched information asymmetry between many senders and receivers is a vital aspect of disclosure that also needs to be recognized.

Insurance supervisors need to be aware of other influences on the marketplace when establishing disclosure requirements and to strive for consistency between their own requirements and the requirements of other stakeholders. Insurance supervisors also need to keep in mind their specific supervisory obligations.

Supervisory authorities have roles to play in establishing disclosure requirements, reviewing the information that is disclosed by those they supervise to assess its appropriateness and compliance with requirements, and properly managing the information that the supervisory authority itself collects, analyzes, and discloses. Adequate systems and processes should exist to support the performance of these tasks.

Supervisory authorities may consider it appropriate to assist market development and stakeholder education by themselves disclosing information to various stakeholders. Their feedback of information to the industry can provide important input to insurers’ management, although care must be taken to ensure that commercially sensitive information is not revealed. Supervisory authorities can also provide information, typically via websites and consumer brochures, directed specifically toward policyholders and potential policyholders, with the objective of improving consumer knowledge and education. Some examples of this approach can be seen on the Mexican Comisión Nacional de Seguros y Fianzas (CNSF) website, the Chilean Superintendencia de Valores y Seguros (SVS) website, and the Financial Information Delivered Online (FIDO) website, supported by the Australian Securities and Investment Commission (ASIC), which focuses on providing financial tips and improving financial awareness of consumers. These websites are included in the reference list.

Disclosure is an evolving area, and much work remains to be done to bring standards of disclosure to the level desired by the marketplace and to ensure consistency and comparability within and among jurisdictions. The discussion in Joint Forum (2004) highlights the evolution of appropriate practices of disclosure throughout the financial services industry. It also makes the point that the insurance sector can learn from other financial services sectors.

The IAIS roadmap indicates that work is expected to be undertaken in the area of public disclosure as part of the overall approach to assessing insurer solvency (IAIS
This work needs to be consistent with the current work of the International Accounting Standards Board in its development of public financial reporting, which affects insurers in many jurisdictions.

The IAIS has also indicated that it will release a new standard on disclosure in 2006 or 2007. This will replace the two existing standards and also address disclosure of the technical performance and risks of life insurers.

**Exercises**

9. Repeat the pretest and compare your initial and current responses. In particular, review any changes you have made in the reasons supporting your choices.

10. Provide appropriate responses to the pretest questions, and, in cases where you have not, review the relevant sections of the module.
F. References

Examples of disclosures on insurer websites:

Australian non-life insurer: See the Insurance Australia Group Limited (IAG) website, www.iag.com.au, for an example of the public disclosure made by a leading Australian insurer. See, in particular, the “Reports and Results” section, which includes both current and archived annual reports and other corporate materials.


Canadian life insurer: Sun Life Financial. See www.sunlife.ca and www.sunlife.com for retail and corporate information, respectively.

Examples of disclosures on supervisory websites:

Australia: Financial Information Delivered Online (FIDO) website, www.fido.asic.gov.au, which is supported by the Australian Securities and Investment Commission (ASIC).

Chile: Superintendencia de Valores y Seguros (SVS), www.svs.cl.

Mexico: Comisión Nacional de Seguros y Fianzas (CNSF), www.cnsf.gob.mx.
Appendix I. ICP 26

**ICP 26 Information, disclosure, and transparency toward the market**

The supervisory authority requires insurers to disclose relevant information on a timely basis in order to give stakeholders a clear view of their business activities and financial position and to facilitate the understanding of the risks to which they are exposed.

**Explanatory notes**

26.1. Public disclosure of reliable and timely information facilitates the understanding by prospective and existing stakeholders of the financial position of insurers and the risks to which they are subject, regardless of whether they are publicly traded or not.

26.2. Supervisory authorities are concerned with maintaining efficient, fair, safe, and stable insurance markets for the benefit and protection of policyholders. When provided with appropriate information, markets can act efficiently, rewarding those insurers that operate effectively and penalizing those that do not. This aspect of market discipline serves as an adjunct to supervision.

26.3. Regular disclosure can facilitate the smooth functioning of the insurance markets. For example, when timely public disclosure exists, market participants are less likely to overreact to negative information about an insurer.

26.4. Greater disclosure entails increased costs, which may be direct or indirect. For example, companies may experience a competitive disadvantage from increased disclosure of proprietary information. These costs must be weighed against the potential benefit of increased disclosure required by any standards.

26.5. The supervisory authority takes action, if necessary in coordination with other relevant bodies, to ensure effective and relevant disclosure.

**Essential criteria**

a. Insurers are required to disclose information on their financial position and the risks to which they are subject. Specifically, information disclosed should be:

- Relevant to decisions taken by market participants
- Timely so as to be available and up-to-date at the time those decisions are made
- Accessible without undue expense or delay by the market participants
• Comprehensive and meaningful so as to enable market participants to form a well-rounded view of the insurer
• Reliable as a basis on which to make decisions
• Comparable between different insurers
• Consistent over time so as to enable relevant trends to be discerned.

b. Information includes quantitative and qualitative information on financial position and financial performance and a description of:

• The basis, methods, and assumptions on which information is prepared (and comments on the impact of any changes)
• Risks exposures and how they are managed
• Management and corporate governance.

c. Insurers are required to produce, at least annually, audited financial statements and make them available to stakeholders.

d. The supervisory authority monitors the information disclosed by insurers and takes the necessary actions to ensure the compliance with disclosure requirements.

**Advanced criterion**

e. Information includes quantitative information of relevant risk exposures.
Appendix II. Answer key

Pretest

1. Reasonable.
2. Not reasonable. However, the supervisory authority should have the power to penalize insurers that are demonstrated to disclose inaccurate information, which implies it needs to have the ability and capacity to verify disclosed information.
3. Not reasonable.
4. Not reasonable.
5. Responses depend on the specifics of the particular jurisdiction and personal experience.

Exercises

1. To what extent do insurers in your jurisdiction satisfy essential criteria a–d of ICP 26?

Responses depend on the specifics of the particular jurisdiction.

2. To what extent does your supervisory authority have in place methodologies, processes, and expertise to assess the practices of insurers operating in your jurisdiction with regard to the essential criteria of ICP 26?

Responses depend on the specifics of the particular jurisdiction.

3. To the extent that an insurer does not satisfy some of the essential criteria of ICP 26, what powers and practices does your supervisory authority have in place to direct and ensure compliance with these criteria?

Responses depend on the specifics of the particular jurisdiction.

4. The introductory section of this module identifies a number of other ICPs in which disclosure plays an important role. Identify the cell or cells of the stakeholder matrix (figure 1) in which these ICPs should be placed.

Specific ICPs (see section A):

- ICP 9: Insurer-to-supervisor, supervisor-to-supervisor, insurer-to-market
- ICP 12: Insurer-to-supervisor
- ICP 13: Supervisor-to-Insurer
• ICP 24: Insurer-to-intermediary, intermediary-to-policyholder
• ICP 25: Insurer-to-policyholder, policyholder-to-insurer
• ICP 27: Insurer-to-insurer, policyholder-to-insurer
• ICP 28: Policyholder-to-insurer.

5. A senior executive of an insurer in your jurisdiction has called to protest that your requirement that a risk management plan be submitted within the next three months is unreasonable, as it will cost too much to produce. How do you respond? If the executive has made a good case due to the complexity of the requirements, how far would you be willing to compromise and why?

Risk management is a core competency for insurers. If they do not have a plan, they have failed this test. The major issue is not the production of the plan but the potential consequences if it is not produced. The requirement to disclose a plan to the supervisory authority has highlighted this risk and issue. Suggest that he get on with producing an acceptable plan!

6. Outline the key criteria for assessing the usefulness of disclosed information.

In section D, see the subsection on criteria for assessing the usefulness of disclosure.

7. A financial information service provider is proposing to publish comparative unit prices for unitized (variable) investment products and suggests that this will provide investors with a clear guide to performance and enable them to purchase the most appropriate products. Do you believe that such information will be both appropriate and sufficient to support the investors' decisionmaking? Explain your reasons.

No. This is an example of partial disclosure. While the provision of unit prices effectively outlines the movement in net asset value for each unit, it does not address the question of how many units the investor holds. If the number of units declines because some are redeemed to pay for fees (a common structure, which is valid and acceptable with appropriate disclosure), then the value movement of the investor's original investment is not fully reported. It is also an example of basing future performance expectations on past history, which is generally regarded as poor or even inappropriate practice. The particular needs of the investor are not considered: it is presumed that investment performance is the only objective, and this is not always the case, as investors' risk profiles, objectives, tax positions, and other obligations should be considered as well. This example demonstrates the complexity and breadth of issues that can arise in assessing the appropriateness of information that is disclosed.
8. Review the annual reports of several major insurers in your jurisdiction and compare their disclosures with each other and with the items discussed in this section of the module.

Responses depend on the specifics of the particular jurisdiction.