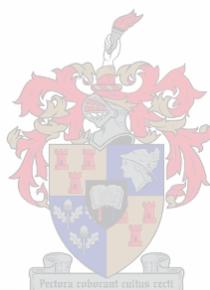


**AN ASSESSMENT OF THE COMPARABILITY OF FINANCIAL REPORTING
BY SOUTH AFRICAN LONG-TERM INSURERS**

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Declaration

I, the undersigned, hereby declare that the work contained in this assignment is my own original work (except where acknowledgements indicate otherwise) and that I have not previously in its entirety or in part submitted it at any university for a degree.

Johannes Petrus van den Berg

Date:

Abstract

Existing long-term insurance financial reporting practices are heavily based on regulatory foundations. Although the reporting requirements of the long-term insurance industry are unique, there is currently no comprehensive, up to date Financial Reporting Standard in South Africa for long-term insurers. The demand for increased disclosure in the financial statements of long-term insurers increases the importance of the basic accounting principles for these companies as embodied in the Framework for the Preparation and Presentation of Financial Statements, namely comparability, relevance, accuracy and understandability of financial reporting.

The SAICA Long-Term Insurance Interest Group discussed the withdrawal of AC121 Disclosure in the Financial Statements of Long-Term Insurers and the replacement thereof by way of other guidance. Ultimately the Accounting Practices Committee has firmly stated that it will not tolerate the ongoing implementation of AC121 because it contradicted a number of other accounting statements and indeed overrode those statements. With this in mind and taking into account the program of harmonising South African accounting standards with International Accounting Standards, it insisted that AC121 be withdrawn and replaced by guidance notes only.

The current lack of authoritative South African guidance on financial reporting by long-term insurers results in the potential compromise of the basic qualitative characteristics of comparability and relevance in their financial statements, as certain disclosures are voluntary rather than required.

The aim of the research was to assess the impact of the lack of authoritative South African financial reporting guidance relating to South African long-term insurers on the basic financial statement characteristic of **comparability**.

A literature study was undertaken and a checklist for disclosure in the long-term insurance industry was drawn up. The objective was to highlight areas of non-comparable disclosure for which financial reporting standards should be created in order to provide guidance on financial reporting by South African long-term insurers and, where possible, to suggest guidance. Financial statements of selected South African long-term insurers were reviewed and “measured” against the checklist in order to make an assessment of comparability.

Currently the disclosure of industry-specific items differs significantly amongst long-term insurance companies in South Africa. The comparability test (on information disclosed in the 2002 annual reports of the selected companies) and the research done on industry-specific items identified by this test indicated the extent of this non-comparability within the South African long-term insurance industry.

In view of the recent withdrawal of AC121 and the results of the comparability test, there is reason to believe that each long-term insurer in South Africa discloses what it believes is right and what it believes the industry is required to disclose. This results in significant non-comparability between the financial statements of South African long-term insurers.

The author recommends that a long-term insurance industry accounting statement in the AC500 series should be issued, which should provide the appropriate guidance not only to preparers of financial statements, but also to other users of financial statements in the long-term insurance industry, until such time as the international accounting project relating to long-term insurers is complete. Some work will be required to update and/or amend a “new AC121” for the AC500 series.

Uittreksel

Die huidige praktyk vir finansiële verslagdoening van langtermynversekeraars berus grotendeels op 'n regulatoriese grondslag. Hoewel die vereistes vir verslagdoening van die langtermynversekeringsbedryf eiesoortig is, bestaan daar tans in Suid-Afrika geen omvattende hedendaagse Finansiële Verslagdoeningstandaard vir langtermynversekeraars nie. Die vraag na groter openbaarmaking in die finansiële state van langtermynversekeraars verhoog die belangrikheid van basiese rekeningkundige beginsels vir hierdie maatskappye soos vervat in die Raamwerk vir die Voorbereiding en Aanbieding van Finansiële State, naamlik vergelykbaarheid, relevansie, akkuraatheid en verstaanbaarheid van finansiële verslagdoening.

SAIGR se Langtermynversekering Belangegroep het die onttrekking van RE121 Openbaarmaking in die Finansiële State van Langtermynversekeraars en die vervanging daarvan deur middel van ander riglyne bespreek. Uiteindelik het die Komitee vir Rekeningkundige Praktyk nadruklik bepaal dat dit nie die voorgesette implementering van RE121 verder kan onderskryf nie, omdat dit teenstrydig is met 'n aantal ander rekeningkundige standpunte en in werklikheid daardie standpunte ter syde stel. Met dien verstande en met inagneming van die harmoniseringsprogram om Suid-Afrikaanse rekeningkundige standaarde in harmonie met Internasionale Rekeningkundige Standaarde te bring, is daarop aangedring dat RE121 onttrek en slegs deur rigtinggewende riglyne vervang word.

Die heersende gebrek aan gesaghebbende Suid-Afrikaanse riglyne oor finansiële verslagdoening deur langtermynversekeraars lei tot die potensiële kompromie van die basiese kwalitatiewe eienskappe van vergelykbaarheid en relevansie

in hul finansiële state, aangesien sekere openbaarmaking vrywillig eerder as verplig is.

Die doel van die navorsing was 'n bepaling van die impak wat die gebrek aan gesaghebbende riglyne vir Suid-Afrikaanse finansiële verslagdoening met betrekking tot Suid-Afrikaanse langtermynversekeraars op die basiese kenmerk van **vergelykbaarheid** van die finansiële state het.

'n Literatuurstudie is onderneem en 'n toetsstaat vir openbaarmaking in die langtermynversekeringsbedryf is opgestel. Die doelwit was om die soeklig te laat val op terreine waar openbaarmaking nie vergelykbaar is nie, waarvoor standarde vir finansiële verslagdoening geskep moet word ten einde riglyne te verskaf oor finansiële verslagdoening deur Suid-Afrikaanse langtermynversekeraars en om waar moontlik, voorstelle hiervoor aan die hand te doen. 'n Oorsig van finansiële state van geselekteerde Suid-Afrikaanse langtermynversekeraars is onderneem en aan die toetsstaat "gemeet" ten einde die vergelykbaarheid te beoordeel.

Teenswoordig verskil die openbaarmaking van bedryfspesifieke items aansienlik tussen langtermynversekeringsmaatskappye in Suid-Afrika. Die vergelykbaarheidstoets (volgens inligting wat in die 2002-jaarverslae van die geselekteerde maatskappye verstrek word) en die navorsing wat gedoen is oor bedryfspesifieke items wat deur hierdie toets geïdentifiseer is, toon die omvang van hierdie nie-vergelykbaarheid binne die Suid-Afrikaanse langtermynversekeringsbedryf.

In die lig van die onlangse onttrekking van RE121 en die resultate van die vergelykbaarheidstoets, is daar rede om te glo dat elke langtermynversekeraar in Suid-Afrika openbaar wat volgens sy oortuigings reg is en wat hy glo van die bedryf verlang word om te openbaar. Dit lei tot beduidende nie vergelykbaarheid tussen die finansiële state van Suid-Afrikaanse langtermynversekeraars.

Die skrywer beveel aan dat 'n rekeningkundige standpunt vir die langtermynversekeringsbedryf in die RE500-reeks uitgereik word, wat die toepaslike riglyne behoort te voorsien nie net aan diegene wat finansiële state voorberei nie, maar ook aan ander gebruikers van finansiële state in die langtermynversekeringsbedryf, tot tyd en wyl die internasionale rekeningkunde projek met betrekking tot langtermynversekeraars afgehandel is. 'n Sekere mate van werk sal nodig wees ten einde 'n "nuwe RE121" vir die RE500 reeks by te werk of dit te wysig.

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Chapter 1

Introduction

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1.1 Background

The South African long-term insurance industry controls a substantial portion of the institutional investments in the South African economy and is also the custodian of the savings and retirement provision of many a citizen of the country.

The demutualisation, listing and internationalisation of some of the major role-players in the industry have resulted in a drastic increase in the demand for disclosure by these companies. As a result of this, most insurers now provide more comprehensive financial information to the users of their financial statements.

Sir David Tweedie, Chairman of the International Accounting Standards Board (IASB), stated: "While the United States' accounting standards are widely seen as the most comprehensive in the world, some deficiencies exist. Adoption of tougher international standards could solve that problem" (PricewaterhouseCoopers, 2003a: 4).

Against the background of the demutualisation and internationalisation in the industry and the concern of the IASB about the adequacy of Generally Accepted Accounting Practice (GAAP) in the United States, the adequacy and authority of the formerly used South African Statement of Generally Accepted Accounting Practice AC121 Disclosure in the Financial Statements of Long-Term Insurers (SAICA, 1994) is drawn into question.

Existing long-term insurance financial reporting practices are heavily based on regulatory foundations. Although the reporting requirements of the long-term insurance industry are unique, there is currently no comprehensive, up to date Financial Reporting Standard in South Africa for long-term insurers. The demand for increased disclosure in the financial statements of long-term insurers

increases the importance of the basic accounting principles for these companies as embodied in the Framework for the Preparation and Presentation of Financial Statements (SAICA, 2004a), namely comparability, relevance, accuracy and understandability of financial reporting (Von Wielligh, 2003).

Some of the latest updates to insurance-related accounting statements across countries were issued in the following years:

- United States: In6 Insurance, October 2001 (FASB, 2001).
- Canada: 4210: Life Insurance Enterprises: Specific Items, November 2001 (CICA, 2001).
- United Kingdom: SORP – Accounting for Insurance Business, December 1999 (ASC, 1999).
- Australia: AASB 1038 – Life Insurance Business, November 1998 (AASB, 1998).
- South Africa: AC121 – Disclosure in the Financial Statements of Long Term Insurers, February 1994 (SAICA, 1994).

It is clear that if we compare the issue date of AC121 to other major international insurance accounting statements, it is evident that the South African statement was issued relatively long ago and therefore has the greatest potential of being outdated.

According to the Draft Statement of Principles: Insurance Contracts (DSOP) issued by the IASB in November 2001 (IASB, 2001), the following are recognised as reasons why an insurance accounting and financial reporting standard is necessary:

- The insurance industry is an important and increasingly international industry;

- There is currently great diversity in accounting practices for insurers. Practices in a number of countries differ significantly and vast differences can be found amongst practices of enterprises in the same country;
- The International Accounting Standards do not currently address specific insurance issues and it is not obvious how an enterprise should deal with these issues; and
- The existence of such a standard may help insurance supervisors in their efforts to approach certain aspects of insurance regulation in ways that are consistent between countries and with regulation of the banking and securities sectors.

A study by West in 1999 indicated that the extent of financial reporting by South African long-term insurers over the period 1993 to 1997 (before demutualisation of long-term insurers) was insufficient compared to international benchmarks (West, 1999). Currently the presentation and disclosure guidance specifically relevant to South African long-term insurers is contained in:

- The Long-Term Insurance Act No. 52 of 1998 (Government of the Republic of South Africa, 1998);
- Statement of Generally Accepted Accounting Practice AC121 Disclosure in the Financial Statements of Long-Term Insurers issued by the South African Institute of Chartered Accountants (SAICA, 1994);
- SAICA Guide on the application of AC133: Financial instruments: recognition and measurement, to liabilities arising from long-term insurance contracts (SAICA, 2003b); and
- Various Professional Guidance Notes issued by the Actuarial Society of South Africa (ASSA, 2001a, 2001b, 2002).

In this regard, the South African situation is by no means different from that of other major economies such as the United States and the aforementioned statement by Sir Tweedie would likewise be applicable to them.

The IASB recognised the need for transparency and comparability in the insurance industry and an insurance financial reporting standard is one of their high priorities. They have initiated a project in order to produce International Accounting Standards on Insurance Reporting. The objective of this project is transparency, consistency and comparability of the financial reporting of insurers. The project comprises two phases that should be effective from 2005 (Phase I) and 2007 (Phase II) respectively.

In March 2004 the International Financial Reporting Standard IFRS4 – Insurance Contracts (IASB, 2004) based on the international ED 5 (IASB, 2003), was issued. The proposals in this first part of the two-step insurance project introduced a definition of an insurance contract and indicate the IASB's expectations regarding valuation and disclosure of these contracts in practice (De Beer, 2003).

The SAICA Long-Term Insurance Interest Group discussed the withdrawal of AC121 and the replacement thereof by way of other guidance. Ultimately the Accounting Practices Committee has firmly stated that it will not tolerate the ongoing implementation of AC121 because it contradicted a number of other accounting statements and indeed overrode those statements. With this in mind and taking into account the program of harmonizing South African accounting standards with International Accounting Standards, it insisted that AC121 be withdrawn and replaced by guidance notes only (Strachan, 2004a).

It seems that SAICA's approach is currently to follow closely what happens internationally and then to react to it locally. This would seem to be the most

logical approach, but it means that a final exposure draft for our long-term insurance industry would only be available by 2007.

This SAICA approach to closely following international developments and the early adoption of these developments, can also be to the disadvantage of South African GAAP, as we do not directly take part in the international discussions and preparation for adoption that assists in a smooth transition.

The current lack of authoritative South African guidance on financial reporting by long-term insurers results in the potential compromise of the basic qualitative characteristics of comparability and relevance in their financial statements, as certain disclosures are voluntary rather than required.

The users of general purpose financial statements include present and potential investors, employees, lenders, suppliers and other trade creditors, customers or clients, the government and its agencies, and the public. These users must be able to compare the financial statements of an entity over time in order to identify trends in its financial position and performance, and to compare the financial statements of different enterprises in order to evaluate their relative financial position, performance and changes in financial position (SAICA, 2004a).

Accounting policies and practices can vary significantly amongst South African long-term insurers for the elements of financial statements that are not covered by existing South African Statements of Generally Accepted Accounting Practice. The differences in accounting policies and practices used by South African long-term insurers also potentially compromise understandability of their financial statements to users.

1.2 Research objective

The international Draft Statement of Principles: Insurance Contracts (IASB, 2001) as well as IFRS4 – Insurance contracts (IASB, 2004) have been developed internationally by the IASB. ED165 Insurance Contracts – Phase I (SAICA, 2003a) is our local equivalent of the international IASB Phase I process, and both ED5 and IFRS4 specifically address insurance contracts. However, the author believes that more than just “insurance contracts” are in need of financial reporting guidance.

Preparers of financial statements, auditors, investment analysts, standard setters and shareholders cannot afford to wait until 2007 for an updated long-term insurance accounting standard. With four financial year-ends before 2007 and the same number of interim reports, users cannot rely on the standard of reporting of the long-term insurance industry if they experience difficulty in comparing the financial statements of companies within the industry.

AC121 (SAICA, 1994) provided basic guidance on presentation and disclosure in the financial statements of long-term insurers. This research will attempt to prove that South African long-term insurers are creating their own disclosure best practices based on different international examples and are disclosing what they believe users need. These disclosures often compromise comparability of financial reporting by these insurers.

The aim of the research is therefore to assess the impact of the lack of authoritative South African financial reporting guidance relating to South African long-term insurers on the basic financial statement characteristic of **comparability**.

The objective is to highlight areas of non-comparable disclosure for which financial reporting standards should be created in order to provide guidance on

financial reporting by South African long-term insurers and, where possible, to suggest guidance.

1.3 Research method

The following method was followed for this research:

- a) A literature study of previous local and international research on presentation and disclosure in the financial statements of long-term insurers was undertaken in order to define the concepts, terms and accounts that are specific to the long-term insurance industry (“industry-specific”). This was done in order to provide a sound basis for the assessment of industry-specific disclosure and concepts in the further stages of the research.

The potential impact of the current IASB developments around the insurance industry, the international Draft Statement of Principles: Insurance Contracts (IASB, 2001), the recently released IFRS4 – Insurance Contracts (IASB, 2004), as well as the local Exposure Draft 165 (ED165) Insurance Contracts (SAICA, 2003a) were also reviewed.

- b) A checklist was drawn up to be used as a measure of items that can be expected to be disclosed in the annual financial statements of South African long-term insurers.

In the 2003 annual Excellence in Corporate Reporting survey by Ernst & Young (Coppin, 2003), insurance companies were rated as follows:

- | | | |
|------------------------|---|-----------|
| • Firstrand (Momentum) | - | Excellent |
| • Sanlam | - | Good |
| • Liberty | - | Good |

- New Africa Capital - Good
- Old Mutual - Adequate

None of the South African long-term insurers featured in the Top 10 (highest) category, while Firstrand managed to be mentioned in the Excellent (second best) category.

The 2002 financial statements of Sanlam Limited and Liberty Group Limited were used as a starting point in creating a checklist for the following reasons:

- There is a strong similarity between the annual financial statements of the two companies;
- Sanlam was awarded the first position in the insurance sector in 2002 (with Liberty second) and Liberty first in 2003 (with Sanlam second) in the annual Investment Analysts Society of South Africa (IASSA) Awards, for the best reporting and communication to the investment community (IASSA, 2003) and;
- The Excellence in Corporate Reporting survey, as mentioned earlier in this chapter, focuses mainly on Corporate Reporting (King-reporting requirements) for all South African companies, whilst the IASSA (whose members use the financial statements for analysis purposes) focus on the accounting disclosure and reporting, presentation and comparability within the insurance industry.

As the review progressed and items were found that were not included in the original checklist, the checklist was updated in order to render it complete and accurate. (These items were marked as “Extra” in Appendix A.)

- c) Financial statements of selected South African long-term insurers were reviewed and “measured” against the checklist in order to make an assessment of comparability.

The following areas of the annual reports for each of the companies were compared:

- Balance sheet;
- Income statement;
- Statement of changes in equity;
- Cash flow statement;
- Accounting policies;
- Notes to the financial statements; and
- Embedded value/Achieved profits report.

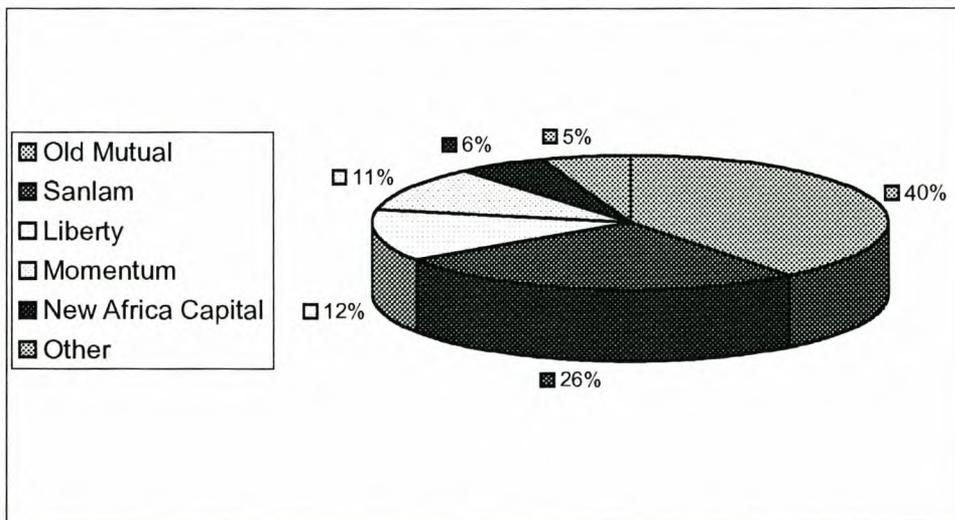
The Annual Reports of South Africa’s top five long-term insurers based on Total Assets for the year ended 2002 were used in the comparability test. They were:

- Old Mutual plc Annual Report 2002 (Old Mutual plc Annual Report, 2002);
- Sanlam Limited Annual Report 2002 (Sanlam Limited Annual Report, 2002);
- Liberty Group Limited Annual Report 2002 (Liberty Group Limited Annual Report, 2002);
- Momentum Group Annual Report 2002 (Firststrand Group Limited Annual Report, 2002); and
- New Africa Capital Annual Report 2002 (New Africa Capital Annual Report, 2002).

Total Assets was used as a selection criterion as the five companies that were selected, represented 94,55% of the South African long-term insurance assets as at 31 December 2002 (PricewaterhouseCoopers-Global, 2003), and have been significantly dominant in the industry in the recent past.

Table 1 provides an overview of the total assets of the South African long-term insurance industry.

Table 1 - Long term insurance assets per company (31 Dec 2002)



Source: PricewaterhouseCoopersGlobal (PricewaterhouseCoopersGlobal, 2003)

- d) The comparability test identified some material long-term insurance industry-specific items of financial statements that were not covered by the former AC121 Disclosure in the Financial Statements of Long-Term Insurers (SAICA, 1994), or for which there was no guidance regarding preferred treatment in other existing accounting statements.

The results of the comparability test were stratified by categorising items as either:

- A. Industry-specific material items found to be treated differently, that could lead to potential disparity (the focus of this research);
or
 - B. Industry-specific items found to be treated differently, but which were not material, or Non-industry-specific items found to be differently disclosed (outside the scope of this research).
- e) The potential level of disparity in the financial reporting of the material industry-specific items (Category A) was assessed by evaluating the different methods of presentation and disclosure used by the five companies selected and the impact on comparability was evaluated.
- f) Suggested solutions were proposed in view of the differences found, to ensure that industry-specific items would be comparable in the future. These suggestions were based on the information gathered during the literature study and on relevant international guidance.

1.4 Value of the research

The research evaluates the extent and adequacy of disclosure by South African long-term insurance companies, with a view to encourage an increase in the extent of disclosure of useful, relevant and comparable financial information and a possible revision of the current financial reporting standards relating to long-term insurers.

In particular, it will be useful to:

- Preparers of financial statements of long-term insurers, by making them aware of the implications of selecting and applying different accounting policies and practices;
- Auditors, in identifying the elements of the financial statements of long-term insurers that are exposed to a high level of audit risk due to disparity in financial reporting;
- Investment analysts, in understanding the risk associated with the vast array of accounting policies and practices currently available to be applied by listed South African long-term insurers and the high risk elements of the financial statements of these companies; and
- Standard-setters of South African GAAP. In the near future, AC121 Disclosure in the Financial Statements of Long-Term Insurers (SAICA, 1994) should be updated and re-issued for the long-term insurance industry and be brought in line with the IASB project for long-term insurers.

1.5 Brief overview of the remainder of the dissertation

An introduction (Chapter 2) gives the reader insight into existing financial reporting guidance for the South African long-term insurance industry, the latest developments in financial reporting guidelines, and a background on international developments.

The qualitative assessment of comparability (comparability test) that was done by using the annual financial statements of the five selected long-term insurers is described in detail (Chapter 3). The elements of difference that were identified and filtered to illustrate the material industry-specific factors that have an impact on comparability of financial reporting, is extracted in this chapter.

The potential level of disparity in financial reporting of the items identified in the comparability test is assessed and the impact on comparability discussed (Chapter 4). Specific attention is given to recognition, measurement, presentation and disclosure differences, by revealing the different bases and methods used by the five selected companies and comparing them to the AC121 (SAICA, 1994) requirements.

The current IASB developments regarding the insurance industry are taken into consideration during the assessment of the material industry-specific items, by looking at, inter alia, the recently released Draft Statement of Principles: Insurance Contracts (IASB, 2001), IFRS4 – Insurance Contracts (IASB, 2004), as well as comments by the Steering Committee of the international insurance project. The potential impact on the future of insurance reporting, an “updated AC121” and the impact on insurers in South Africa are evaluated (Chapter 5).

Recommendations for improvement of South African guidance are made where possible.

A brief summary concludes this research and possibilities to extend this research in future is explored (Chapter 6).

Chapter 2

The current insurance accounting picture

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2.1 Current South African insurance GAAP

During a visit to South Africa in January 2002, Sir David Tweedie, chairman of the International Accounting Standards Board (IASB), confirmed that Statements of South African GAAP were of a high quality. The South African Institute of Chartered Accountants (SAICA) is also committed to continue raising accounting standards in South Africa. The SAICA Technical Unit captured this in its mission statement (De Beer & Prinsloo, 2002: 9): “to be recognised as a leading authority that participates in national and international processes in order to achieve globally recognised standards for the benefit of members, associates and the public at large.”

This can be contrasted to a quote from an article by Hattingh in *Accountancy SA* (Hattingh, 2003: 27-29), when approached by one of the large banks to advise them on whether or not collection costs should be taken into account when calculating bad debts. He contends that the accounting statement is not clear on whether the net or gross cash flow should be used when discounting cash flows from debtors, and therefore not unambiguous.

The example mentioned by Hattingh is the same as is often found in the insurance industry. This is where the accounting statement applicable to the industry-specific item does not provide adequate guidance for resolving industry-specific issues.

After Hattingh studied the whole accounting statement from paragraph 1 to paragraph 174 it was concluded that collection costs should not be taken into account. In an effort to confirm this point of view, opinions from three large auditing firms were obtained. Two replied negatively and one replied affirmatively. It was proposed to write to the IASB, the source of GAAP and the people who make the science, to obtain a ruling on the matter. The reply was: “We set standards. We do not interpret them. Get an opinion from your auditors.”

The article ends with the following paragraph: I prefer to quote my friend, philosopher and deep thinker on matters of accounting, Deon Joubert from Eskom, who once said: “GAAP is a manmade science”.

From this example it can be seen that achieving comparability in any financial reporting environment or in any industry is by no means straightforward, even if there are appropriate industry GAAP statements and opinions from auditors. This very same “manmade science” currently also exists in our long-term insurance industry.

There is often a gap between stakeholders’ information requirements and the information that is actually made available to them by companies. Traditional financial reporting is limited in its ability to portray a holistic picture of any company.

There is also a growing expectation for a more proactive approach that puts corporate financial performance in context. This means providing investment analysts and other stakeholders with more of the information that management uses to run the business, allowing them to better evaluate its performance (Smith, 2003: 5). It was already reported in 1999 that compliance by listed companies with statements of GAAP in South Africa was poor (Hattingh, 1999).

The two main reasons for this poor compliance were said to be:

1. Preparers were ignorant of the new statements.
2. There was no legal requirement to comply with the new statements.

The GAAP Monitoring Panel was a step in the right direction and the JSE has since then published regulations that require listed companies to comply with Statements of GAAP.

Recent media reports have stated that the government is employing business experts to attract investments to South Africa. It is generally accepted that sophisticated international investors will not invest in companies if such companies do not meet the highest level of international GAAP compliance and transparency (Coppin, 2003).

At the present time, in addition to significantly diverse accounting practices for insurers between various countries, insurance accounting practices differ significantly amongst insurers within the same country and with the accounting practices of other industries. For international organisations, these differences create inefficiencies in financial reporting.

In the last few years preparers of financial statements in South Africa have had to cope with a large number of both new and revised accounting statements in addition to interpretations of accounting statements. It has also been a challenge for users of financial statements and auditors to keep abreast of statements that have become both longer and more complex.

2.2 Development of International Guidance

The IASB last discussed Phase II of the insurance standard in January 2003. The intention is to start discussing Phase II again in mid-2004 and to complete an exposure draft by 2005 (Ernst & Young, 2003a).

Given the current dissatisfaction with insurance accounting in many countries, the author believes many national standard setters will strongly consider incorporating the proposals in the ultimate insurance IAS into their local GAAP. As a result, the Steering Committee's proposals are of current relevance to all insurers, even if at the moment they do not prepare financial statements under IAS.

The Steering Committee's overriding priority was to develop a standard on accounting for insurance contracts that is consistent with the (IASB) conceptual framework definitions of assets and liabilities. This framework reflects the growing support for the "fair value" accounting model amongst many national bodies, including the UK Financial Services Authority (FSA) and US Financial Accounting Standards Board, members of whom have played an active role in the drafting of the DSOP (PricewaterhouseCoopers, 2002b: 2-3).

Although some guidance is already available (DSOP, IFRS4, ED5), important areas are still under review, including the vexing issue of disclosure. All aspects of the DSOP are "tentative" and thus subject to debate, revision and ultimate approval by the IASB.

The DSOP's focus is the accounting treatment of insurance contracts, but it is recognised that the project will also need to deal with the presentation of financial statements.

Key features of the DSOP (PricewaterhouseCoopers, 2000: 1-8) include:

- Confirmation that profit recognition will be determined by the movement between the valuation of the assets and liabilities recognised by an insurance company ("an asset and liability approach"). Any assets and liabilities recognised must fall within the definitions set out in the IASB Framework, hence capitalised costs such as deferred acquisition costs (DAC) are not permitted.
- Introduction of a new definition of an insurance contract with no distinction between life and general insurance.
- All financial assets will be measured in line with IAS 39 on Financial Instruments, which will result in investments held at either amortised cost or fair value.

- Liabilities arising from insurance contracts will be calculated using a discounted cash flow technique. Current proposals indicate that an Entity Specific Value might be used.
- To value guarantees and options included in contracts, option pricing model techniques must be used.

An accounting treatment based on the Steering Committee's initial proposals will represent a fundamental change from current practice in South Africa. Many of the principles are in line with the way in which many life insurers internally manage profitability, and are unlikely to cause concern regarding internal reporting. Although IFRS will have a positive impact on disclosure requirements, key features of the IFRS could lead to reported earnings results that bear little relation to those seen today.

In South Africa IFRS4 will already apply from 2005, and it clarifies the definition of an insurance contract in terms of IAS32 (AC125 Financial Instruments: Presentation and disclosure) and IAS 39 (AC133 Financial Instruments: Recognition and Measurement). While the more fundamental changes as outlined earlier will follow under Phase II, the impact of Phase I is expected to be significant for insurance contracts. These include new disclosure requirements and some required modifications to the existing insurance accounting practices.

As a result, the implementation of these proposals is expected to present a major challenge for all insurance companies. Financial reporting on this basis is likely to require significant changes to accounting and actuarial models and information systems and shifts in areas such as product design and capital allocation. The performance report to shareholders could also change significantly. These developments are therefore important to senior management of these companies.

2.3 Background on current International Insurance Guidance

According to Sir David Tweedie the objective of the IASB is to have a single set of high-quality global standards. It is taking a worldwide look to see which country has the best answer in any particular area, and this will be the solution it chooses. There are certain issues for which no particular country has a suitable answer, in which case the IASB and the national standard-setters will work together to try to find one. The secret to restoring confidence in the markets is to have no surprises and full transparency.

Tweedie goes on to say that if confidence in the markets is the objective, we must have good standards, good auditing and good enforcement. If a standard is ambiguous, the IASB must take responsibility to change it; if an interpretation is required, the IASB will provide it (PricewaterhouseCoopers, 2002a: 1-2).

Management of global insurance companies needs to redefine the presentation and disclosure of their financial performance so that it is more readily understood, is uniform across the countries in which it operates, and is effective in communicating its financial condition to the competitive global markets. Homogeneous standards are an essential tool for the management of a global, diverse organisation to ensure uniformity in managing risk and profitability across its operations.

Investors and analysts insist on being able to evaluate and benchmark a company's financial performance to its global competitors, with jurisdictional differences becoming transparent. Furthermore, numerous insurance regulators have added their voices to the request for consistency in standards across countries and the various financial services industries such as insurance.

International Accounting Standards (IAS) are accepted by many stock exchanges as the basis of reporting for foreign issuers (either with or without a reconciliation

to local GAAP). The acceptability of IAS is likely to increase following the recent recommendation from the International Organization of Securities Commissions (IOSCO) that its members should allow multi-national issuers to use IAS for the preparation of their financial statements. In addition, many countries already endorse IAS as their own, either without amendment or else with minor additions or omissions (Masters, Hofmann & Van der Hoeven, 2002: 8-10).

The use of IAS will expand further in the future. The EU recently announced proposals to require most EU companies, including insurers, to prepare their consolidated financial statements in accordance with IAS. This requirement will come into effect by 2005. Firms using US GAAP as their primary reporting basis will be exempt until 2007 (Masters, *et al.*, 2002: 12).

In respect of unlisted insurers (and other financial institutions), the EU has suggested that member countries may wish to require compliance with IAS to facilitate comparability and to ensure efficient and effective supervision.

There has been renewed interest and focus on profit reporting by companies following the collapse of Leisurennet, Regal, Worldcom and Enron. The need for international accounting and financial reporting standards on insurance contracts has also been debated for a number of years.

Recognising the need for global insurance GAAP, the IASC commenced a project on insurance accounting in 1997, and in November 2001 the IASC's Steering Committee on insurance issued an extremely detailed and thorough discussion paper on accounting for insurance contracts (Ernst & Young, 2003a). ED 5 and IAS 39 – Insurance and Investments Contracts: Understanding the Implications for Phase I was issued and the paper ultimately led to the development of the new International Financial Reporting Standard (IFRS) for insurance contracts, IFRS4 – Insurance Contracts issued in March 2004.

IFRS4 – Insurance Contracts (IASB, 2004), the IASB's finalised framework for the transitional Phase I of the move to International Financial Reporting Standards (IFRS), provides a stable, albeit temporary, platform that will enable insurers to concentrate on practical implementation issues.

The recently released IFRS4 – Insurance Contracts, mainly addresses insurance contracts (their definition, recognition, measurement and disclosure) and does not address the rest of the accounting issues relevant to the long-term insurance industry (Long-term Rate of Return, policyholder and shareholder split or new business). All entities that issue policies that meet the insurance contract definition in IFRS4 should consider the new standard in their conversion plans. However, IFRS4 will not apply to policyholder accounting (French, 2004: 14).

In the first phase (Phase I), the IASB focused on enhanced disclosures for insurance contracts. The extent of any new quantitative or qualitative disclosures should be of interest to the users of annual financial statements. According to Nossel, Muir & Penny (2003), these enhancements relate to:

- Assumptions used in calculating liabilities and a liability adequacy test.
- Significant terms and conditions of main types of insurance contracts sold that have implications on the amount, timing and certainty of cash flows.
- Insurers' objectives in managing risk including reinsurance and asset/liability matching.
- Information about insurance risk e.g. sensitivity to key variables, exposures gross and net of reinsurance, concentration of insurance risk.
- Actual claims compared to previous estimates.
- Separate disclosure for reinsurance contracts.
- Separate disclosure for insurance and investment contracts.

According to Frits Bolkstein, EC Internal Market Commissioner (Masters, Morton & Mittal, 2002: 13) the International Accounting Standards will introduce a new era of transparency and put an end to the current "Tower of Babel" in financial reporting by insurers. It will help firms to compete on equal terms when raising capital on world markets and allow investors and other stakeholders to compare companies' performance against a common standard.

The initial phase was designed to make limited improvements to accounting practices, and provide insights into the key risk drivers and sensitivities of insurance contracts. The plans set out in IFRS4 are relatively modest in comparison with the overhaul of insurance accounting envisaged under Phase II.

2.4 Presentation of financial statements

There is a great need for development of detailed guidance on the presentation of financial statements for long-term insurers, and it is noted that if a fair value regime is adopted, then consideration should be given to segregating elements of performance between value adjustments and a more traditional reporting basis (Eccles & Nelligan, 2003: 18).

In 1998, PricewaterhouseCoopers Inc. commissioned Market & Opinion Research International (MORI) to carry out a global study of the perceptions regarding corporate reporting in insurance (Value and Reporting in the Insurance Industry). The respondents included 26 insurance companies, 51 institutional investors and 36 sell-side analysts who follow the industry (MORI, 1998).

The survey revealed considerable market scepticism and dissatisfaction with the quality of current financial reporting. Only two of the 17 respondents declared scarcely more than a moderate understanding.

Greater transparency of disclosures, with the clear separation of the results of new business from those of pre-existing business, will focus the spotlight on any “false optimism” in the setting of assumptions by the management of companies.

In future we may see enhanced disclosures in areas such as the assumptions used in determining insurance provisions, sensitivity analysis, risk mitigation effort, information on solvency requirements and other key performance indicators (Nossel, *et al.*, 2003).

A significant concern is that the adoption of a fair value regime will increase the volatility in reported earnings. Kees Storm, Chairman of the Executive Board of AEGON, states that, because of the valuation of assets and liabilities at market values, we will see great swings in results that policyholders and shareholders will not understand. He believes that companies will show incomprehensible results that give no information on their long-term performance at all (Clark & Plas, 2002: 24).

2.5 Conclusion

Apart from IFRS4, there is currently no global GAAP for insurance accounting. Local GAAP for insurance accounting varies substantially between countries, which makes it difficult for users of financial statements to make meaningful comparisons between countries and between the different local insurance companies. Local insurance GAAP often does not satisfy the requirements of the user and this may act as a barrier to creating investor confidence.

The author believes that volatility will be best addressed by explicitly identifying the sources of this volatility in the income statement and associated notes. Management will need to learn to communicate more effectively how short-term fluctuations in financial position fit in with their long-term strategy.

The author believes that the global use of IFRS will contribute to comparability, as this is one of the major objectives of these standards. As described, these global IFRS standards will hopefully improve comparability, but there are a few year-ends for South African insurers before the end of 2007.

The author strongly supports the need for an IAS on insurance presentation and disclosure. In the next chapter it will be proved that the insurance industry discloses industry-specific items that are unique to this industry. It is these unique items that are in need of industry-specific guidance. Much further work is however needed to develop a standard that has widespread support from investors, insurers, regulators, national standard setters and other users of financial statements.

Chapter 3

Identification of industry-specific items in the annual financial statements of South African long-term insurers

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3.1 Background on the comparability test

The research method followed was described in Chapter 1. Appendix A contains the comprehensive results of the qualitative comparability test.

In Chapter 1 it was mentioned that the annual reports of South Africa's top five long-term insurers (based on Total Assets) for the 2002 financial year were used in the qualitative comparability test. All but two are listed on the Johannesburg Securities Exchange (JSE) SA. Momentum Group Limited represents the insurance interests of the Firstrand Group Limited that is listed on the JSE. Metropolitan Life is a wholly-owned subsidiary of listed Metropolitan Holdings Limited (previously New Africa Capital Limited).

For the 2002 financial year, the directors of these insurance companies should have been using AC121 Disclosure in the Financial Statements of Long Term Insurers (SAICA, 1994) as the GAAP statement for their industry-specific accounting issues.

3.2 Results of the comparability test - Industry-specific items

The focus of this research is on items specific to the long-term insurance industry ("industry-specific"). It was evident from the comparability test performed, that there are material insurance industry-specific items that are not covered by AC121. These are the items for which one would expect to find guidance in an accounting statement specifically for long-term insurers.

By measuring each of the five companies against the checklist, differences were found in the recognition, measurement, presentation and disclosure of industry-specific items.

They are items such as:

- i. The unique life fund and related earnings of a long-term insurer;
- ii. Premium income, policy benefits and outward reinsurance premiums or reinsurance recoveries;
- iii. Long-term Rate of Return (LTRR);
- iv. Financial instruments and the implications for long-term insurance businesses;
- v. Valuation issues;
- vi. Total assets under administration and total funds received from/paid to clients;
- vii. New business funds received; and
- viii. Accounting for the deferred tax implications of capital gains tax in the long-term insurance industry.

These items are further discussed in Chapter 4.

If a quantitative comparison had been done of amounts disclosed, other issues relating to their fair presentation might have emerged. This research assumes that reliance for this aspect can be placed on auditors' opinions on the relevant financial statements. This study focuses on a qualitative comparison between the disclosure of industry-specific items.

3.3 Results of the comparability test – Non Industry-specific items

Although it is not the primary focus of this research, certain non-industry-specific items were identified in the comparability test for which disparity existed in financial reporting.

As can be expected, every company included in the study has its own focus and disclosure style when it comes to presenting financial results. A comparison of

the financial statements indicated that terminology and definitions for similar items were different.

Examples include:

- Goodwill compared to Intangible assets;
- Non-distributable reserves compared to showing Foreign currency translation, Investment and Merger reserves separately;
- Retirement benefits are presented differently from company to company; and
- The financial statements should be placed in the order required by AC101 Presentation of Financial Statements (SAICA, 1998). AC101 places the balance sheet before the income statement. Both Sanlam and Old Mutual still placed the income statement first at 31 December 2002.

Accounting statements other than AC121, already address some of the other items that were found to be treated differently, and one would therefore expect disclosure to be in accordance with these other GAAP statements. This is, however, not always the case, as can be seen when comparing the financial statements of long-term insurers.

Examples of such items are:

- Provisions, contingent liabilities and contingent assets (AC130). Provisions in particular are disclosed very poorly in the financial statements of Sanlam, compared to the more detail and more thorough descriptions of the other companies;
- Property, Plant and Equipment (AC123) are not always material in the financial statements of companies in the long-term insurance industry, as can be seen in the extent of disclosure in the financial statements of Sanlam and Liberty. Momentum is the only company that discloses the

useful lives of each of the asset classes. In the recent international improvements to IAS, which follows a component approach, each material component of an asset with a different useful life or a different pattern of depreciation is depreciated separately and appropriate disclosure per asset class should be provided;

- Sanlam and Liberty disclose “Owner-occupied properties” whereas Old Mutual, Momentum and Metropolitan do not mention it. While the disclosure of Investment Properties differs significantly from company to company, it may however be argued that the latter three companies do not occupy any of their own properties for administration of own business. The users of the financial statements must rely on the proper application of the relevant GAAP statement (AC135) to result in the proper disclosure of owner-occupied properties;
- Although the disclosure of Earnings per share (EPS) is addressed by a GAAP statement, AC104, disclosure differs significantly between the companies. Old Mutual bases its EPS on Long-term rate of return (LTRR) (see LTRR in Chapter 4) while New Africa Capital was one of the few to show an “Earnings per income statement” to “Headline earnings” to “Core headline earnings” reconciliation.
- The disclosure and presentation of investments, financial instruments and debentures differ significantly from one company to another, as there are different risks related to the financial instruments of each company. The disclosures of these financial instruments are covered by AC125 and the newly issued IAS 32.
- Retirement benefits will rarely be the same between two companies and the comparability test indicated that the AC116 disclosure of each of the companies was unique. The disclosure of retirement benefits is already covered by a separate accounting statement, AC116, and one would expect the insurance industry to comply well with the requirements.
- The capitalisation of computer development costs occurred in the financial statements of Liberty, Momentum and New Africa Capital, but

not in Sanlam's or Old Mutual's financial statements. This area is covered by AC129 Intangible assets and AC432 Intangible assets – web site costs.

- Related parties disclosures differ significantly, but new international guidance will give companies more guidance on the required disclosures.

It is the responsibility of directors to prepare financial statements in accordance with the requirements of statements of GAAP and the Companies Act. Hattingh (Hattingh, 2001: 19) states that: "the annual report is the window through which the user determines whether or not the results presented are reliable and transparent. If the window is dirty, scratchy and scrappy, the results will not be believed and the share price will be downgraded". The author assumes that there are reasons for the non-industry-specific items found to be disclosed differently. The different disclosures found for non-industry-specific items falls outside the scope of this research.

3.4 Conclusion

It is impossible to cover all practical industry scenarios in accounting statements. It is often said that if one wants to deal with 80% of the issues, the standard would for example comprise 50 - 60 pages; whereas if one wanted to include 95%, it would extend to 300 pages (Ntombela, 2003).

As the individual disclosure items were measured during the comparability test - for disparity in recognition, measurement, presentation and disclosure - and industry-specific differences were found between the five selected companies, the individual industry-specific items were classified into one of eight main material long-term insurance industry-specific items of disclosure.

For the long-term insurance industry to have eight material industry-specific items not covered by a (industry-specific) GAAP statement, opens the door for significant disparity in financial reporting. The disparity found in the eight industry-specific items identified will be evaluated and discussed in the next chapter (Chapter 4).

This disparity is, in the view of the author, equivalent to leaving a considerable portion of industry-specific disclosure without an accounting statement to provide guidance to the preparers and users of these financial statements.

Chapter 4

Comparison of financial reporting of industry-specific items

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4.1 Introduction

The purpose of this research is to establish whether the South African Statement of Generally Accepted Accounting Practice AC121 Disclosure in the Financial Statements of Long Term Insurers (SAICA, 1994), adequately covers the industry-specific items identified in the comparability test and, if not, whether new long-term insurance industry-specific financial reporting standards should be created.

In this chapter, the disparity in recognition, measurement, presentation and disclosure found in the eight industry-specific items identified by the comparability test will be evaluated and discussed and recommendations will be made where possible.

Throughout the chapter the following references are used in all Tables:

- SLM - Sanlam Limited Annual Report 2002;
- OML - Old Mutual plc Annual Report 2002;
- LIB - Liberty Group Limited Annual Report 2002;
- MOM - Momentum Group Annual Report 2002; and
- NAC - New Africa Capital Annual Report 2002.

4.2 The unique life fund and related earnings of a long-term insurer

The life fund is fundamental and relevant to the economic substance of any long-term insurer.

Balance sheet and cash flow statement

Table 2 shows the balance sheet and cash flow statement differences found during the comparability test.

Table 2 – Balance sheet and cash flow statement disclosure

	SLM	OML	LIB	MOM	NAC
The Group balance sheet contains assets and liabilities of policyholders and shareholders, but discloses the total Policyholders' funds and Shareholders' funds separately	✓	✓	✓	✓	✓
Separate information regarding the Shareholders' assets and liabilities is provided in addition to the policyholders' assets and liabilities (in either an additional balance sheet or a note)	✓	x	✓	x	x
Cash flow statement distinguishes between cash flows of shareholders' funds and policyholders' funds	✓	✓	x	x	x

The separation between policyholders and shareholders is what makes financial reporting by a long-term insurer unique. The life fund (policyholders' liabilities) is central to the understanding and evaluation of the insurer's financial statements and the importance of the disclosure of the fund downplays the disclosure of items that are often important in other industries, such as Property, Plant and Equipment and Inventory.

The income statement of a long-term insurer contains cash flows (premiums and benefits), followed by one transfer to policyholder funds, which is not comparable to the revenue, cost of sales and expenses used by other industries.

AC121 paragraph .07, defines the "life fund" as follows (SAICA, 1994):

"The life fund comprises amounts set aside in the business that, together with future premiums in respect of existing unmatured policies and other future income, are available to meet the costs of expected benefit payments and future expenses in respect of such policies, and where applicable, for making allocations to shareholders' funds for the payment of dividends.

"The life fund is supported by an actuarial valuation and may include other surpluses available to policyholders or shareholders. Amounts set aside in the life fund may include appropriations from shareholders' funds depending on the

amounts required according to the actuarial valuation of existing unmatured policies. The life fund may, in the case of a mutual insurer, be more appropriately described as the policyholders' fund."

There are different descriptions for policyholder' liabilities and reserves (life fund) in the balance sheets of South African long-term insurers:

- Sanlam: Long-term policy liabilities
- Old Mutual: Long-term business provision and Technical provision for linked liabilities
- Liberty: Life funds
- Momentum: Long-term liabilities
- New Africa Capital: Long-term insurance fund

The only guidance on disclosure of the life fund is contained in paragraph .14 of AC121 (SAICA, 1994):

"Details of movements in the life fund should distinguish between:

- transfers from or to the income or operating statement,
- the aggregate gains or losses on revaluation and on disposal of investments, and
- all other material movements."

It is clear from Table 2 that the unique policyholders' funds and shareholders' funds used in the long-term insurance industry and the different disclosure methods used by companies can lead to disparity. This disparity caused by the life fund also affects the income statement and the disclosure of accounting policies applied in calculating earnings.

Table 3 – Profit entitlement disclosure

	SLM	OML	LIB	MOM	NAC
Profit entitlement policies					
General reference to existence of profit entitlement policies	✓	✓	✓	✓	x
More detail on profit entitlement policies	✓	x	✓	✓	x

In respect of income recognition and the cash flow statement, the accounting policies in the financial statements of all five selected long-term insurers state the following: “Premium income is accounted for when due from policyholders or received in cash.” Premiums are “transferred” to the life fund and operating profit results from the “transactions” in the life fund.

The life fund is therefore the place where the shareholder earnings from policyholder business are calculated and all the related accounting or profit entitlement policies followed should be adequately disclosed.

Earnings from long-term insurance activities are governed by the profit entitlement policies of the insurer. These policies describe the manner in which shareholders earn their profits from the various long-term insurance activities performed by the insurer, and can be linked to specific product lines (Von Wielligh, 2004: 208). They are similar in purpose to accounting policies, although they relate specifically to earnings arising from transactions between shareholder and policyholder funds.

Table 3 illustrates that, although most companies refer in general to the existence of profit entitlement policies, not all companies provide an adequate level of detail on these policies to be useful and comparable.

The life fund and second-tier margins

Table 4 – PGN 104 and second-tier margins

	SLM	OML	LIB	MOM	NAC
Policy liabilities:					
Valuation in accordance with PGN 104 of the Actuarial Society of South Africa	✓	✓	✓	✓	✓
Second-tier margins are included	✓	✓	✓	✓	✓

The value of the life fund liability (“the liability”) is actuarially calculated, based on the principles of Professional Guidance Note 104 (PGN 104) Life offices – financial soundness valuation (ASSA, 2001a). As shown in Table 4, all five companies indicated that they valued policy liabilities in accordance with PGN 104 and all the companies selected included second-tier margins as part of the liability.

In the introduction to PGN 104 (ASSA, 2001a) it is stated that the intention of the financial soundness valuation is to give a prudent realistic picture of the overall financial position of the insurer. It also states that a minimum level of financial resilience is introduced by way of:

- Best estimate assumptions of all parameters increased by prescribed as well as second-tier margins for profit-reporting purposes, and in addition,
- Compliance with capital adequacy requirements for financial soundness purposes.

The actuarial valuation assumptions and principles will therefore determine the amount of earnings reported by a long-term insurer. Based on profit recognition principles in other industries, it would be expected that the amount of premium income not required to meet liabilities and future expenses in respect of a policy would be reflected as earnings.

For this purpose, AC121 par. 18 defines it correctly (SAICA, 1994):

“Taking into account the nature of life insurance, it is important to recognise that profit does not arise in the customary sense from the excess of income over expenses, but rather from the comparison of the estimated surplus of assets over liabilities between one estimating date and the next. This is determined by the insurer’s actuary. In the case of proprietary insurers, the directors, using their judgement and based on the advice of the actuary, and subject to the insurer’s articles, may then decide how much of the surplus of assets over liabilities can be released to shareholders’ funds.”

Directors of insurance companies are responsible to ensure that good standards of underwriting and reserves are maintained. The level of prudence applied by directors and actuaries in setting margins should, however, not distort the actual performance of the company by allowing undue reserves to be created during highly profitable years and the subsequent release of these reserves during periods of poor investment performance or poor underwriting results (“profit smoothing”).

The profit reported by most long-term insurers is, however, often smoothed. This is mainly the result of the additional margins (second-tier margins) added to the calculated liabilities allowed by PGN 104 (ASSA, 2001a).

Paragraph 48 of The SAICA Guide on the Application of AC133 Financial instruments: Recognition and Measurement, to Liabilities arising from Long-term Insurance contracts (SAICA, 2003b) states that:

“The most reliable measure of fair value is a quoted market price or the price of recent transactions where a deep and liquid market exists. Where this is not the case, AC133 paragraph 97 indicates that a reliable measure of fair value can be

determined where there is ‘...an appropriate valuation model and for which data inputs to the model can be measured reliably...’”

Paragraph 49 of the SAICA Guide (SAICA, 2003b) goes further: “In the case of investment contracts issued by long-term insurers there is no deep and liquid market and transactions are not sufficiently frequent to provide a realistic valuation. Therefore an estimation model should be considered.”

It seems that second-tier margins in liabilities will still be allowed on financial instruments, as paragraph 52 of the SAICA guide (SAICA, 2003b) states that:

“In choosing the FSV method the Statutory Actuary will need to review all relevant assumptions in the light of the above to ensure that the combination of best estimate assumptions plus any margins results in a reasonable measure of fair value ...”

From 1 January 2005 IFRS4 will be applicable to insurance contracts and IAS39 will be applicable to investment contracts. Insurance contracts will be valued on the Financial Soundness Valuation basis (as was previously done) and investment contracts will be reported at fair value without margins (for some products first-tier margins will still be used).

First-tier margins (prescribed margins) are required by PGN 104, and are deemed necessary to allow for a certain level of prudence. It is evident from Table 4 that all the selected insurers include second-tier margins.

A reduction of second-tier margins could lead to an increase in net asset value, but a decrease in the value of in-force business. The impact on disclosed embedded value is that there will be an immediate release of earnings, which will lead to a slight increase in valuation, as the cash flows would not need to be discounted. This would affect all the companies in the comparability test.

To ensure transparency and credibility of profit reporting in the long-term insurance industry, the guidance in respect of second-tier margins should be reconsidered. These second-tier margins should aim to provide a realistic picture of the emergence of profits on insurance policies.

The AC133 implications for long-term insurers will also have an effect on the Receiver of Revenue. Even if not this year, JPMorgan (Nossel, *et al.*, 2003) suspects that the South African tax authorities would continue to require tax calculations on a basis consistent with profit reporting which would mean they would use AC133 for tax calculations. Whether the tax authorities follow the use of AC133 is important, as elimination of the second-tier margins should increase the transfers to the shareholders' funds and accelerate the payment of tax.

Table 5 – Disclosure of insurance product types

	SLM	OML	LIB	MOM	NAC
Separate group and individual business	✓	x	✓	✓	✓
Information on basic product types included	✓	x	x	x	x

Table 5 indicates that only Sanlam provides information on group and individual business separately as well as descriptive detail regarding policy products.

Table 6 – Disclosure of HIV/Aids reserve and bonus stabilisation reserves

	SLM	OML	LIB	MOM	NAC
HIV/Aids reserve	✓	x	✓	✓	✓
Reduction in earnings caused by using a retrospective HIV/Aids valuation basis instead of a prospective valuation basis	✓	x	x	x	x
Disclosure of bonus stabilisation reserves	✓	x	x	x	x

The HIV/Aids reserve to be applied is prescribed in a table in the actuarial guidance. It is the only reserve that is prescribed in exact detail, whereas other

reserves are determined by the actuaries and approved by the statutory actuary. An item such as bonus stabilisation reserves can lead to income smoothing.

As the measurement of second-tier margins are highly subjective and has a direct impact on earnings (similar to Provisions), the author believes that detailed presentation and disclosure guidance should exist in this regard. The disclosure requirements in respect of second-tier margins should include an analysis of the margins per type of insurance product, a description of any changes in the product that resulted in a change in the level of second-tier margins held and a reconciliation of the movements in the margins for the year. This will allow the users of the financial statements to compare the different margins held between insurers and the effect it has on the earnings.

4.3 Premium income, policy benefits and outward reinsurance premiums or reinsurance recoveries

Format of the Income statement

Table 7 – Income statement disclosure

	SLM	OML	LIB	MOM	NAC
Income statement includes only items related to the shareholders' fund	✓	x	x	x	✓
Income statement relates to both shareholders' and policyholders' funds	x	✓	✓	✓	x
Income statement or notes disclose net income relating to shareholders and policyholders separately	✓	✓	✓	✓	✓
Detail of income and expenses relating to shareholders' and policyholders' funds can be distinguished in income statement and notes	✓	x	✓	x	✓

What makes the life fund and its disclosure even more complicated, is that no guidance exists for reporting earnings on the face of the income statement.

Paragraph .19 of AC121 states that “Disclosure of income or operating statement items should be made using the following accounting principles...” (SAICA,

1994). The paragraph goes on to provide guidance on premiums, benefit payments, gains or losses on investments, new business costs and costs directly related to revenue earned from property investments. There is no reference or guidance to separate disclosure for shareholders and policyholders. In the view of the author proper guidance should be provided as to the disclosure regarding the split between shareholders and policyholders.

Table 7 clearly indicates that Sanlam and New Africa Capital show only shareholders' transactions on the face of the income statement, whereas the income statements of Old Mutual, Liberty and Momentum contain transactions relating to shareholders and policyholders added together.

All the companies, however, disclose net income relating to shareholders and policyholders somewhere on the face of or in notes to the income statement, but the implications for users of what is disclosed on the face of the income statement as opposed to in the related notes are important.

- Sanlam shows "Funds Received from Clients" (policyholders and shareholders). The line just below it shows "Financial services income" (shareholders). Although both items are defined in the accounting policies, there is no reconciliation from one to the other (Sanlam, 2002).
- The income statement of Liberty starts with "Net premium income" (policyholders), less "Claims and policy-owners' benefits" (policyholders), less "Commissions", "Management expenses", "Tax" and "Investment surpluses" – all relating to policyholders. After all these lines, there is "Life fund transfers" (policyholders) and a separate "Revenue earnings attributable to shareholders' funds" calculation (Liberty, 2002).
- The income statements of Old Mutual and Momentum are comparable to the Liberty method.

- New Africa Capital, starts with “Income from insurance business” (Shareholders) (New Africa Capital, 2002), the equivalent of Sanlam’s “Financial services income”. One can possibly argue that Sanlam and New Africa have full disclosure of premium income from policyholders and policyholder benefits paid, in notes to the income statement as required by paragraphs .26 and .27 of AC121, but for the reader to obtain the necessary information, the notes have to be studied in detail.

The author recommends that the appropriate method of disclosure for income reporting should be in the form of guidance for items to be shown on the face of a long-term insurers’ income statement in order to achieve comparability within the industry and, possibly, with other industries.

Reinsurance

Paragraphs .26 and .27 of AC121 state that “Re-insurance premiums/benefits [should be] disclosed separately where material” (SAICA, 1994).

Table 8 – Reinsurance disclosure

	SLM	OML	LIB	MOM	NAC
Reinsurance premiums/recoveries disclosed	✓	✓	x	x	x
Premium income shown net of reinsurance premiums	✓	✓	✓	✓	✓
Policyholder benefit payments net of reinsurance recoveries	✓	x	✓	✓	✓
Outstanding claims/benefits stated net of reinsurance	x	✓	✓	x	x

Reinsurance is set to play an increasingly larger role in capital management as insurers look to manage their capital more efficiently.

Globalisation has accelerated the consolidation of primary insurance companies, resulting in increased retention of risks traditionally reinsured. This negative factor for reinsurers is offset to some degree by the consolidated primary insurers' increased need for more sophisticated risk analysis and coverage (De Villiers, 2002: 14).

There has, more recently, been some concern that the ability of reinsurers to help in reducing primary insurers' regulatory capital requirements has sometimes appeared to depend in part on regulatory arbitrage (including tax arbitrage) and accounting arbitrage (different treatment for accounting purposes of identical risks in the books of primary insurers and reinsurers). There has been a trend towards increased regulatory scrutiny of reinsurance arrangements.

From the disclosure found in the comparability test it can be seen that Sanlam and Old Mutual currently disclose reinsurance premiums and recoveries. Premium income is net of reinsurance and policyholder benefit payments are net of reinsurance recoveries when disclosed by Sanlam, Liberty, Momentum and New Africa Capital. Old Mutual and Liberty are the only two that disclose the fact that outstanding premiums (debtor) and outstanding claims/benefits (creditor) are stated net of reinsurance.

In terms of IFRS4, reinsurance will be subject to the same accounting treatment as insurance, as long as it meets the definition. Gross discounted claims projections and reinsurance recoveries will be shown separately on the accounts, before arriving at a net position. The reinsurance recoveries will be shown as an asset that will be reduced for the risk of default by the reinsurer.

IFRS4 requires gross disclosure of outstanding premiums. Off-setting of reinsurance debtors against outstanding claims and reinsurance creditors against outstanding premiums should adhere to general accounting off-setting rules. This

will be very rarely allowed, as the payments from the reinsurer very seldom occur at the same time of the claim payment or debtor collection.

In view of the increasing trend of scrutiny of reinsurance arrangements, the disclosure of reinsurance in the future might increasingly be regarded as “material” in terms of paragraphs .26 and .27 of AC121, and there will be renewed focus on reinsurance disclosure. Reinsurance is an important part of risk management and will be of great concern to the shareholders.

The author recommends that more detailed disclosure requirements and guidance should be provided for reinsurance disclosure in the financial statements of South African long-term insurers.

4.4 Long-term Rate of Return (LTRR)

Table 9 – Long-term Rate of Return

	SLM	OML	LIB	MOM	NAC
PRO FORMA LTRR HEADLINE EARNINGS (R million)	✓	OML	x	x	x
Pro forma LTRR headline earnings per share based on the long-term rate of return (LTRR) (cents per share)	✓	Headline earnings are LTRR	x	x	x

There have been numerous discussions and debates regarding the acceptability of the use of Long-term Rate of Return (LTRR) by long-term insurers. The principle of LTRR on investments, is that an expected pre-tax rate of investment return, that is to be earned over the longer-term, is calculated on all “free” investment assets. “Free” assets are shareholders’ funds investment assets that are not required to cover policy liabilities. (Du Toit, 2003). The effect is to eliminate short-term fluctuations in investment returns from earnings.

Paragraphs 245 to 248 of The United Kingdom Statement of Recommended Practice (SORP) – Accounting for Insurance Business (ASC, 1999) - relate to

“The Longer Term Rate of Investment Return” and provide the methods to be used, the investments to be included in the calculation and how the rate should be determined.

In a JSE Securities Exchange South Africa (JSE) circular issued on 21 February 2003 the JSE stated that they had been advised by the GAAP Monitoring Panel that “the ‘Long-term investment return on shareholders’ funds adjustment in the income statement is contrary to South African Statements of Generally Accepted Accounting Practice (“GAAP”)” (Doel, 2003).

The circular further states that the income statement should have “no adjustments in relation to the so called long-term rate of return (LTRR)” (Doel, 2003).

Sanlam’s disclosure of the LTRR complies with all relevant requirements:

- It is presented below the income statement prepared in accordance with GAAP;
- A pro forma earnings figure based on the LTRR is disclosed (clearly separate from the income statement); and
- A pro forma earnings per share figure based on the LTRR earnings is disclosed with the other Earnings per Share (EPS) data, but clearly indicated as not being EPS calculated in accordance with AC104.

Whereas Sanlam applies the circular appropriately, Liberty, Momentum and New Africa Capital refrained from disclosing LTRR at all, which is also acceptable. Old Mutual on the other hand does not disclose its LTRR separately and their headline earnings are based on LTRR. The primary listing of Old Mutual is on the London Stock Exchange where this is acceptable.

The JSE circular requires the following (Doel, 2003):

- The basis of determination of the LTRR, i.e. the percentage applied should be disclosed;
- A reconciliation of pro forma LTRR earnings to earnings per the income statement should be disclosed;
- Additional disclosure may not be made with the pro forma earnings figure: it should be made in the notes to the financial statements; and
- The headline earnings per share must be prepared in accordance with circular 7/2002 on Headline Earnings, i.e. no inclusion of the LTRR adjustment.

The JSE circular states that in terms of GAAP, the LTRR earnings do not have to appear within the audited part of the annual report at all, but the JSE is mindful of comparability issues with companies which have their primary listings elsewhere. This section probably relates to the Old Mutual primary listing in the United Kingdom.

The long-term rate of return is a good guideline and a benchmark for users of the annual financial statements of long-term insurers to determine the long-term average earnings. An example is in the Independent Fundamental Research online company results analysis, where the analyst does not look at normal headline earnings, but rather states that: "Headline earnings based on a 12% long-term rate of investment return, improved by 8%..." (Independent Fundamental Research, 2003).

Sanlam uses this tool very effectively to disclose its earnings as is allowed by the JSE circular.

The author recommends that the appropriate method of disclosure for LTRR earnings reporting should be GAAP guidance for items to be shown on the face

of a long-term insurer's income statement or in a LTRR note in order to achieve comparability within the industry.

4.5 Financial instruments and the implications for long-term insurance businesses

The disclosure of risks related to financial instruments is determined by AC133 and AC125. Appendix A contains the full details of which risks were disclosed by each of the respective companies.

The qualitative comparability test indicated that the different companies provide disclosure of the following industry-specific risks:

Table 10 – Financial instruments disclosure

	SLM	OML	LIB	MOM	NAC
Securities lending	✓	x	x	✓	x
Underwriting risk	✓	x	✓	✓	✓
Legal risk	✓	x	✓	x	x
Claims risk	x	x	✓	x	x
Operational risk	x	x	✓	✓	x
Tax risk	x	x	✓	x	x
Property risk and hedging risk	x	x	x	x	✓
Capital adequacy risk	✓	x	✓	x	✓

AC125, entitled "Financial instruments: Presentation and Disclosure" and AC133, entitled "Financial Instruments: Recognition and Measurement", deals with the use of fair values as a recognition and measurement basis for financial instruments and the presentation and disclosure of the instruments in the financial statements. The South African equivalents of IAS 32 and IAS 39, which are the International Accounting Standards relating to Financial Instruments: Presentation and Disclosure, and Financial Instruments: Recognition and Measurement, include guidance on the concepts of disclosure and fair value.

When asked what the IASB could do to reduce the complexity in the area of financial instruments, Sir David Tweedie answered: "In the short term, not much. We have had various problems with the inherited IAS 39" (PricewaterhouseCoopers, 2002b: 4).

JPMorgan (Nossel, *et al.*, 2003) believes that the three main possible implications of AC133 for pure investment products of long-term insurers are:

- 1) A reduction in the use of second-tier margins;
- 2) A possible reduction in use of negative rand reserves; and
- 3) A change in requirements for calculating minimum maturity guarantee reserves.

From the risks identified in Table 10, it is clear that there are a lot of different viewpoints as to what the directors of the selected insurers see as risks relating to financial instruments and what they disclose. Not all companies include the same risks and AC121 should provide guidance for disclosure of the industry-specific risks that a long-term insurer is typically exposed to, to complement AC125.

AC133 should not have a significant impact on the valuation of financial assets on the insurers' balance sheets, as most assets are already valued at fair value. The more important impact should be on the liability side of the balance sheet. The statement does not apply to insurance contracts, but it does apply to financial instruments e.g. pure unit-linked contracts.

Impact on Headline earnings

Table 11 – Investment surpluses excluded from headline earnings

	SLM	OML	LIB	MOM	NAC
Investment surpluses excluded from headline earnings	✓	N/A	✓	x	x

With the latest renewed focus on headline earnings, the main issue is that the company can either:

- record investment income, realised *and unrealised* capital gains and losses on shareholder funds fully in the income statement and include them in headline earnings, or
- include only investment income and *realised* gains in the income statement, whereas unrealised investment gains or losses are not recorded in the income statement, but taken directly to equity in the statement of changes in equity.

For the second option, all realised and unrealised capital gains or losses will then be excluded from headline earnings. The method of handling this is at the discretion of the company, but needs to be applied consistently from year to year.

It appears as if Sanlam (SLM) and Liberty (LIB) will exclude unrealised gains and losses from headline earnings in the future. This method was adopted and appropriately disclosed by Sanlam and Liberty for their interim results in June 2003.

The author recommends that guidance on the inclusion or exclusion of these realised and unrealised gains and losses from headline earnings should be provided to ensure consistency between companies and for consistency of financial statements over time.

4.6 Valuation issues

It is interesting to note that AC121 does not refer to any Professional Guidance Note (PGN) in order to link the accounting statements with actuarial guidelines.

Critical valuation methods were compared between the companies selected. It appears that there is a degree of inconsistency in the methods used and this impacts earnings reporting, as mentioned in section 4.2.

Embedded value/Achieved profits

Table 12 – Embedded value and Achieved profits disclosure

	SLM	OML	LIB	MOM	NAC
Embedded value/Achieved profits					
Audited report	✓	✓	✓	✓	✓
Basis of preparation disclosed	✓	✓	✓	✓	✓
Detail of embedded value earnings provided	✓	✓	✓	✓	✓
Assumptions provided (valuation assumptions and discount rates)	✓	✓	✓	✓	✓
Sensitivity analysis on value of in-force business	✓	✓	✓	✓	✓
Sensitivity analysis on value of new business	✓	✓	✓	✓	✓

Embedded value is defined as the net assets of the shareholders at fair value, plus the value of the in-force business, less the cost of capital at risk. The financial soundness valuation includes both prescribed and discretionary margins, which can be expected to emerge as profits in the future. The value placed on these future expected profits after taxation is the value of the in-force life business (Sanlam, 2002).

The Embedded value per share can be used to determine the net asset value of a long-term insurer as it gives a value to the in-force business book of the insurer. Analysts often use Embedded value per share for a long-term insurer and compare it to the Price/Earnings valuation per share of other industries.

In the comparability test done in this research, the impact of the newly adopted PGN 107 can clearly be seen as the Embedded value section of the disclosure comparison is of a very high quality and according to the requirements of PGN 107 Life Offices – Embedded value: Measurement and Disclosure (ASSA, 2001b).

In the United Kingdom it is market practice for life insurers to publish supplementary “achieved profits” information in addition to the accounts required by UK GAAP. As Old Mutual's primary listing is in the United Kingdom, the company adhered to the Association of British Insurers (ABI) guidance on disclosing information on “achieved profits” in their 2002 Annual Report. This replaces the embedded value information provided in previous years (Old Mutual plc. Annual Report, 2002: 12).

The achieved profits method focuses on earnings before tax. The achieved profits methodology is based on an attribution of the assets of a life assurance company between those backing long-term insurance contracts and the residual assets representing unencumbered capital (Old Mutual plc., 2002).

A general conclusion follows at the end of section 4.6, but from Table 12 it appears that sufficient guidance already exists for the disclosure of Embedded value and Achieved profits.

Valuation of minimum maturity guarantees

Table 13 – Capital adequacy requirements (CAR)

	SLM	OML	LIB	MOM	NAC
Capital adequacy requirements (CAR)					
CAR and CAR multiple provided	✓	✓	✓	✓	✓
Details of assumptions	✓	x	✓	✓	✓
Management actions disclosed	✓	x	✓	✓	✓

The CAR issue is applicable to all of the selected insurers as Table 13 shows that all five insurers disclose CAR.

This issue could be material if the entire minimum maturity guarantee was included as a best-estimate liability rather than a combination of best-estimate liability, prescribed margin and an increase in CAR as is suggested in the latest revised guidance note from the Actuarial Society of South Africa (ASSA, 2001a).

At the moment most insurers reserve for minimum investment guarantees using crude methods, e.g. 1% of relevant assets. As a result of reserving for a portion of this liability, the impact of the guarantees on the financial position is reduced.

None of the companies in the comparability test disclosed these minimum guarantees or the methods used to value and present them. Companies do not disclose this reserve separately and it is very difficult to estimate. The guidance note from the ASSA relates specifically to reserving for minimum maturity guarantees (ASSA, 2001a).

The following calculation (Nossel, *et al.*, 2003) shows the potential impact on the valuation if the entire minimum maturity guarantee allowance were considered a best estimate liability. As can be seen, if companies have already allowed for half of the new calculated minimum maturity guarantee using existing crude methods, the overall impact if the full amount were considered a best-estimate liability would be some 1%-2% of embedded value.

Table 14 – Estimating the potential impact of AC133 on reserving for minimum maturity guarantees*(Rand millions)*

	SLM	OML	LIB	MOM	NAC
Estimated market-linked liabilities with underlying guarantees	18,650	15,173	25,962	11,263	361
Estimated smoothed bonus liabilities with maturity guarantees	23,807	30,506	2,220	4,954	6,963
Estimated total liability with maturity guarantees	42,457	45,679	28,182	16,217	7,324
Estimated reserve required under new guidance	170	183	113	65	29
Estimated CAR under new guidance (1.6%)	679	731	451	259	117
Combined impact	849	914	564	324	146
Embedded value (EV) at 31/12/2002	27,087	54,267	15,126	9,876	6,323
Combined impact/embedded value (%)	3.1%	1.7%	3.7%	3.3%	2.3%
50% of combined impact/EV (%)	1.6%	0.8%	1.9%	1.6%	1.2%

Source: JPMorgan estimates, company reports (Nossel, et al., 2003)

It is therefore considered to be the most significant potential adjustment from an embedded value point of view.

The calculation would change over time, because as markets rise or fall, the probability of minimum maturity guarantees having a big impact will change, based on changes in asset levels. It is therefore difficult to say whether this will have a positive or negative impact on earnings. The author agrees that this would all depend on whether the current reserves are higher or lower than the new draft recommended reserves and at the moment it is impossible to determine the impact on current disclosure.

Conclusion

The Embedded value/Achieved profits and valuation of minimum maturity guarantees, are not adequately addressed in the revised PGN103 or PGN 104 and should be. For disclosure purposes, a GAAP statement specific to the long-term insurance industry should address these areas or reference to relevant PGN's should be made in the GAAP statement.

In the near future, valuation issues such as how the split between policyholder and shareholder funds take place, the role of the actuary in reporting requirements for with-profit portfolios, more details on the analysis of surplus and “King II-type” responsibilities of actuaries will also need to be looked at and disclosed in the annual financial statements (Ntombela, 2003).

4.7 Total assets under administration and total funds received from/paid to clients

Total funds received from clients are comparable to turnover or revenue of companies in other industries. Total funds paid to clients are claims and fund terminations that were paid out to policyholders.

Table 15 – Funds received, benefits paid and assets under management

	SLM	OML	LIB	MOM	NAC
Funds received from clients	✓	✓	x	✓	✓
Total premium income	✓	✓	✓	✓	✓
Policyholder benefit payments net of reinsurance recoveries	✓	x	✓	✓	✓
Analysis per product					
Insurance business - Premium income	✓	x	x	x	x
Long term insurance policy benefits	✓	x	✓	✓	✓
Segregated funds not included in the balance sheet	✓	x	x	x	x
Total assets under management and administration	✓	✓	x	x	x

According to the Sanlam accounting policies, the definition of funds received from clients is (Sanlam, 2002):

“Funds received from clients consist of single and recurring long term and general insurance premium income, which are included in the financial statements, as well as unit trust contributions, inflow for assets managed and administered on behalf of clients and non-life insurance linked-product contributions, which are not included in the financial statements as they are funds held on behalf of and at the risk of clients. Transfers between the various types of business, other than those transacted at arm’s length, are eliminated.”

Not one of the other four companies gave a definition or disclosure of what their definition of Funds received from/paid to clients was. Liberty did disclose “Funds received from clients”, “Payments to clients” and “Net flow of funds”, but without a definition of what they regard as funds or flows and what policy they adopted (Liberty, 2002).

Funds received from clients should be disclosed in detail and analysed by the companies in their disclosure as this will convey important information on sources and volumes of business and exposures to certain types of business as well as future earnings potential.

The flows between insurance and asset management entities in the same group should be eliminated during the consolidation process on a consistent basis, to enable users to compare the extremely important disclosure of these items from a group perspective. AC121 should help long-term insurers to define the policy they must adopt for consolidation and this policy should be properly disclosed by the insurers in order to be comparable.

AC121 paragraph .38 refers to “Managed assets” (SAICA, 1994):

“Where the insurer manages assets on behalf of other parties, these assets are not assets of the insurer and therefore are not included in its balance sheet. However, disclosure of that fact and the fair value of these managed assets should be made in its financial statements.”

AC121 makes no reference to funds received from/paid to clients. Particularly in a complex group structure, there should be authoritative guidance as to when an asset under management or a flow of funds should be accounted for and disclosed.

If the total funds received or paid are inconsistent between companies, users will find it difficult to make an accurate estimation for the medium to long term, because the impact of net funds flow for the current year will only be seen in the income or profit in future years.

4.8 New business funds received

Table 16 – New business disclosure

	SLM	OML	LIB	MOM	NAC
New business premium income	✓	✓	✓	x	x
In the case of long term insurance business the value of all new policies that have incepted during the financial year and have received at least one premium is regarded as new business	✓	x	x	x	x
All segregated funds inflows, unit trust inflows and general insurance premiums are regarded as new business	✓	x	x	x	x
New business costs are recognised in the Income Statement when incurred and forms part of the actuarial liabilities in accordance with Actuarial Standards (GAAS)	x	x	✓	x	x

Key:

x - Disclosure not found

For new business, Sanlam states in its accounting policy (Sanlam, 2002):

“In the case of long term insurance business the value of all new policies that have incepted during the financial year and have received at least one premium is regarded as new business.”

Not one of the other four companies gave a definition or disclosure of what their definition of New business was. Liberty did disclose “*New business inflows*”, but without a definition of what they regard as new business and what policy they adopted for recognition of new business (Liberty, 2002).

The Embedded value of new business is an indicator of the value of new business of the current year that will lead to income and profit in the years to

come. A low value of new business indicates lower earnings, while a high value of new business indicates higher earnings in subsequent years.

The value of new business, together with the actual new business funds received, are of great importance when a projection over the next few years is made. The income and profit of an insurer occurs over a number of years and not all in the year when the new policy is issued.

No reference is made in the accounting statement AC121 to new business. In an industry such as the insurance industry, there should be authoritative guidance as to how and when new business should be accounted for and disclosed.

4.9 Accounting for taxation and the deferred tax implications of capital gains tax in the long-term insurance industry

Table 17 – Taxation disclosure

	SLM	OML	LIB	MOM	NAC
Taxation					
SA Life insurance - four-fund method	x	x	x	✓	x
Policy liabilities include:					
Deferred capital gains tax	✓	✓	✓	✓	✓

South African long-term insurers use a unique industry-specific four-fund tax calculation method, but only Momentum refers to this unique method in their accounting disclosure.

Prinsloo states in Accountancy SA of March 2002 (Prinsloo, 2002: 28), that accounting for the deferred tax implications of Capital Gains Tax in respect of policyholder investments is complicated. This is because of the need to maintain consistency between the method that a life company uses for charging its policyholders and the method it uses to reserve for these charges.

From the current disclosures not much can be learnt:

- Sanlam clearly shows its deferred tax as included in the life fund as part of the life fund note.
- Liberty states in their accounting policy that: “The life funds include deferred tax on unrealised capital gains tax in respect of policyholder investments. Deferred tax liabilities are not discounted” (Liberty, 2002).
- Old Mutual discloses: “Comparative figures restated for adoption of Financial Reporting Standard (FRS) 19 ‘Deferred Tax’” (Old Mutual, 2002).
- Momentum discloses that the tax calculation was done on the “SA Life insurance - four-fund method”. In the deferred taxation note a separate line is included for “Capital Gains Tax on unrealised investment surpluses” (Firstrand, 2002).
- New Africa Capital discloses “Capital Gains Tax (CGT) on unrealised and realised gains and on realised losses on shareholders’ investments is included in deferred tax in the balance sheet.” It does however state in the deferred tax note that: “No deferred tax liability has been raised for policyholder capital gains tax as the estimated tax loss exceeds the capital gain” (New Africa Capital, 2002).

As a result, representatives from the long-term insurance industry (through the SAICA Long-term Insurance Project Group) prepared a paper recommending that deferred tax arising from Capital Gains Tax in respect of policyholder investments should be included as part of actuarial liabilities as opposed to being treated as an accounting liability.

An important implication of this is that the deferred tax liability might be discounted, which is contrary to the provisions of AC102 Income Taxes (SAICA, 2004b).

A sub-committee of the SAICA Long-term Insurance Project Group and representatives from the SAICA Accounting Practices Committee debated the recommendation and concluded that the matter has to be brought to the attention of the IASB. The sub-committee should prepare a paper for submission to the IASB Steering Committee on Insurance (Prinsloo, 2002: 28).

The SAICA Accounting Practices Committee and the Accounting Practices Board should also consider this paper with the possibility of expanding it to cover the implications of the non-allowance of discounting of deferred tax on other industries. In the interim, long-term insurance companies should comply with the provisions of AC102 Income Taxes.

As this issue is already being addressed by SAICA, this research includes no proposals in this regard.

4.10 Conclusion

In Chapter 3 the comparability test identified eight material long-term insurance industry-specific items for which authoritative financial reporting guidance would be expected to exist. Everybody - from preparers of financial statements in the long-term insurance industry to users of financial statements of a South African long-term insurer - will have to deal with these eight identified items in some way.

Items such as return and profit reporting, valuation of the liability to policyholders, funds and assets managed, the tax implications of the unique life fund and the disclosure of these items, places great demands on an industry specific accounting statement. It is evident from the tables provided by means of the comparability test and discussion of these tables in Chapter 4, that there is a significant extent of disparity in financial reporting in the South African long-term insurance industry.

The unique life fund creates an accounting requirement for long-term insurers that is radically different from those of other industries in South Africa as well as abroad, as will be indicated in the following chapter. This radically different accounting requirement needs to be addressed by a radically different industry-specific accounting statement.

Chapter 5

The future of insurance reporting

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5.1 Introduction

All over the world accounting standards are converging. The idea is that eventually a single set of global accounting standards will be used to prepare financial statements.

While the IASB has set the direction, companies still have considerable room to create disparity in respect of insurance contracts in key areas. This ranges from the adoption of new accounting bases for insurance contracts to the use of shadow accounting and floating discount rates to achieve some level of matching of assets and liabilities.

5.2 Recognition and measurement regime

One of the major issues is what the recognition and measurement framework for insurance contracts should be. For measuring, the Steering Committee has considered two basic models – a deferral and matching model and an asset and liability model (PricewaterhouseCoopers, 2000: 3).

- The **deferral and matching model** is driven by the profit and loss account. The objective is to match costs with revenues. This leads to the deferral of premiums and the costs of acquisition of business to match the incidence of claims and expenses over the period of the insurance contract.
- The **asset and liability model** is balance sheet driven. It aims to measure assets and liabilities that arise from insurance contracts. Profit emerges as the values of these assets and liabilities change over time.

The Steering Committee does **not** consider a deferral and matching model as consistent with the IASB's framework for the preparation and presentation of financial statements. IAS will seek to measure the assets and liabilities that arise

from insurance contracts, rather than deferring income and expenses. The IASB considers that fair value should be adopted for insurance contracts as they are typically considered to fall within the definition of financial instruments. The mechanism for the move to prospective provisioning is likely, initially at least, to be Entity Specific Valuation (ESV).

ESV seeks to establish the assets and liabilities arising from policies in force, based upon a valuation of the future cash inflows and outflows. This will eliminate the concept of accruals and matching and it implies, inter alia, that all acquisition costs will have to be expensed immediately and all premiums received would be recognised at once (PricewaterhouseCoopers, 2000: 6).

There is strong support for the existing deferral and matching framework from certain countries (notably Germany, France and Japan). Their concerns exist in two main areas (PricewaterhouseCoopers, 2000: 4):

- There is not a sufficiently deep or liquid market for the assets and liabilities arising from insurance contracts which makes a fair value model difficult to apply; and
- Insurance contracts may be more appropriately classified as service contracts rather than financial instruments.

The concerns regarding the lack of a deep and liquid market and the definition of service contracts need to be addressed for the fair value approach to be effective.

5.3 Application of fair values in practice

The definition of fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length

transaction. This has been interpreted as an exit market value ideally determined by reference to a market transaction (PricewaterhouseCoopers, 2000: 5).

In an IASB Update issued April 2003, the IASB reaffirmed a previous decision that an insurer should disclose the fair value of its rights and obligations under insurance contracts from 31 December 2006 (PricewaterhouseCoopers, 2003b: 1).

This could materially change the way in which liabilities are calculated and could preclude the use of the Financial Soundness Valuation method in its current format in favour of international standards. The intention is that the guidelines will be consistent across the world. This could lead to a replacement of or significant changes to PGN104, the relevant guideline of the Actuarial Society of South Africa (ASSA) for calculating liabilities. All five the selected companies in the comparability test disclosed the use of PGN 104 as a standard for their valuations and the replacement of PGN 104 is likely to affect them.

Significant concerns have been raised that there is no market for liabilities under insurance contracts in South Africa or, if there is a market, it is thinly traded.

For most investment assets, use of market values will be in line with IAS 39. For insurance liabilities, ESV is the present value of costs that the enterprise will incur in settling the liability in an orderly fashion over the life of the liability. As such, ESV is conceptually comparable to fair value, though it does not need to rely on a liquid market for liability valuation, which for insurance is effectively non-existent.

Many analysts are concerned about the comparability of financial statements prepared according to IAS and the previous frameworks, especially as the evaluation of earnings and performance will be so markedly different under the

new and old frameworks. Even between ESV and Achieved Profits (AP) techniques (AP is widely used in the UK) there are significant differences.

In the view of the author, the lack of a perfect market does not preclude the use of a fair value model. It is possible to model fair values using information available to individual insurers and parameters driven by market data.

While it is possible to construct fair values for insurance contracts, there are some concerns about the usefulness of financial statements that result from applying too strict a definition of fair value to insurance contracts.

In a recent paper on its preliminary views on measuring financial instruments at fair value, the US standard setter, FASB, has for example stated that insurers would need to value insurance contracts based on a market experience of expenses. A company's own expense experience may be significantly different. An inefficient insurer could ignore its own inefficiencies in calculating profits on the basis that the market could process the business more efficiently (IASB, 2003).

To ensure that objectivity is maintained, it will be necessary for the IASB to develop more practical guidance to arrive at a basis for estimation of fair value, recognising the nature of the product and the lack of a deep market. This will still involve estimation, but should ensure that principles are established which can be applied consistently and, in doing so, will support comparability.

5.4 Embedded derivatives

Following the publication of IFRS4, insurers should consider the implications of the proposed amendments to IAS 39 in relation to the use of the fair value option in the measurement of financial instruments. This amendment, expected to be applicable from 1 January 2005, will limit the application of the fair value option to

instruments that contain embedded derivatives or have other features that indicate that fair value is an appropriate measurement for the instrument (for example the financial liability is contractually linked to assets measured at fair value).

IAS 39 requires an entity to separate some embedded derivatives from their host contract, measure them at fair value and include changes in their fair value in profit or loss. IAS 39 applies to derivatives embedded in an insurance contract unless the embedded derivative is itself an insurance contract within the scope of this statement.

To comply with AC133, embedded derivatives (e.g. minimum maturity guarantees and foreign currency futures) need to be valued at fair value. The main impact on insurers is that minimum maturity guarantees will need to be valued. Actuarial guidelines are currently being drafted for these valuations and these may need to be revised to be consistent with AC133.

In a report issued by JPMorgan in November 2002 (Nossel, Muir & Penny, 2002), they estimated the impact on liabilities and Capital Adequacy Requirements (CAR). It was concluded that the impact on liabilities would be small, but the impact on CAR could be material.

According to AC133, a phased approach will not be allowed and the full extent of the calculated fair value reserve would need to be included in liabilities rather than in CAR. It is expected that this would also apply to the minimum maturity guarantee on with-profits business, as embedded derivatives in insurance contracts (not related to insurance events) also need to be valued.

The impact on embedded value would depend on whether companies can value the liability based on best estimate assumptions or including a first-tier margin. If it is considered to be a first-tier margin, the impact would be much less, as first-

tier margins are assumed to be released in the embedded value calculations, whereas best-estimate liabilities are not released into embedded value until the time that the experience is actually better than the best-estimate assumptions.

5.5 Classification and unbundling of insurance contracts

In South Africa, long-term insurers initially thought they would be excluded from the scope of AC133. This was not the case. A temporary solution was agreed upon between the industry and SAICA until clear guidance from the IASB is provided on the issues raised by the long-term insurance industry. The main concern was the definition of an insurance contract. It was also found that the term “policy” is not defined in any accounting guidance.

IFRS4 Insurance Contracts replaces the indirect definition of an insurance contract in IAS 32 with a positive definition based on the transfer of significant insurance risk from the policyholder to the insurer. According to IFRS4 the definition of an insurance contract is (IASB, 2004):

“A contract under which one party (the insurer) accepts significant insurance risk from another party (the policyholder), by agreeing to compensate the policyholder if a specified uncertain event (the insured event) adversely affects the policyholder.”

Some argue that where the financial risk is in any way greater than the level of insurance risk, for example 51%, then the contract should be treated as a financial instrument.

The uncertainty, or risk, can be explained as the probability that a specified future event in the contract may occur, when the event will occur and how much the insurer will need to pay if the event occurs.

In practice, this new definition of insurance risk could exclude many forms of credit insurance and pre-retirement savings plans, which would instead be accounted for in terms of the financial instruments standard (IAS 39). This new definition also makes **no** distinction between life, health or general insurance contracts – all will be treated in the same way for accounting purposes.

Where a contract contains both an insurance element and a non-insurance element and the separate components are explicitly disclosed to the policyholder or are clearly identifiable from the contract, the Steering Committee recommends that these elements should be “unbundled” and accounted for separately.

Various techniques could be applied in measuring the relative levels of insurance and financial risk. Considering the cash flows arising in the contract, or a discounted cash flow model, will for example produce different answers. Aside from this, it is acknowledged that the level of insurance risk in a contract varies during the course of the contract. It is difficult to determine at what point the classification should consequently occur, but according to IFRS4 and the Draft Statement of Principles, it is apparently accepted that contract classification should take place at inception.

The consequences are that if a contract takes the legal form of insurance and have the principal characteristics of insurance at inception, it should continue to be accounted for as an insurance contract throughout its existence.

However, if the contract does “principally” transfer financial risk, then applying IAS 39 to such contracts would value the liability either at ‘amortised cost’ or at ‘fair value’. IAS 39 would require cash received from premiums to be recognised directly as a financial liability rather than as revenue. Likewise, claims would not be treated as an expense, unless the claim amount was in excess of the provision set aside for the individual contract (Ernst & Young, 2003b).

In general the author agrees that some insurance contracts meet the definition of financial instruments. In the event that the definitions for an insurance contract and a financial instrument remain for the interim solution, more guidance will clearly be required to determine how the term “principally” is to be interpreted.

5.6 Investment Margins

The Faculty and Institute of Actuaries stated their position on the IASC’s Issue Paper on Insurance by saying: “We strongly support the argument that insurance business is reported on a portfolio of policies basis, as this is how the business is priced and managed” (PricewaterhouseCoopers, 2002c: 13).

Investments of funds arising from a contract are a necessary element of insurance which is implicitly or explicitly recognised in product pricing. The main issue is the appropriateness of the discount rate to be used to value the related insurance liability. The philosophy of what discounting achieves is an arcane issue as yet unresolved by the IASC (or FASB).

It appears likely that pressure from the USA will drive towards either a risk-free or a corporate bond rate being used. This again ignores the commercial value of the insurance contract which is currently valued in market transactions inclusive of a margin. Another problem is a lack of market depth and market volumes.

5.7 Specific exclusions

The DSOP states that “an event that is only a change in one or more of a specified interest rate, security price, commodity price, foreign exchange rate, index of prices or rates, a credit rating or credit index or other variable” does not fall within its scope. While this is likely to receive some further refinement, the general direction is accepted (Swift, 2003).

In addition, many policies now considered to be insurance contracts will be specifically excluded, regardless of whether they meet the definition or not, because they are dealt with under other statements. These include (IASB, 2003):

- Employee benefit plans;
- Contingent payments under business combinations; and
- Contracts contingent on the future use of non-financial assets.

5.8 Conclusion

Existing insurance accounting models in South Africa have tended to focus on regulatory needs - policyholder protection in particular - rather than providing the meaningful earnings and performance disclosure ("fair presentation") that would enhance comparability and is required by analysts and investors.

The proposals in the International DSOP would potentially have the advantage of aligning regulatory financial reporting with the more "realistic" discounted cash flow techniques favoured by many market professionals, of which Achieved Profits, Embedded Value and the Entity Specific Valuations are examples. As its architects have argued, the proposals in the DSOP could also improve transparency and comparability with other financial sectors, creating a level playing field in the capital markets that would benefit both insurers and investors in our country (PricewaterhouseCoopers, 2002d: 5-6).

Some concerns about the proposals still remain, particularly in relation to the potential up-front profit recognition and its complexity in comparison to existing accounting requirements. For analysts, more is involved than merely the technical and book-keeping issues. Their ability to assess the performance and strategies of business will depend upon the transparency of the eventual requirements and disclosures and their intelligibility, with the short implementation horizon making intelligibility a real problem in the short-term.

The IASB could possibly consider amending the IAS definitions to avoid some of the issues identified in this chapter. However, a key challenge for the IASB and the industry will be to find other suitable alternatives, as this will drive many of the subsequent accounting issues.

It will be necessary for companies in South Africa to explain to the market what impact the eventual IAS will have on their reported performance. Much more market and analyst communication will be required in the approach towards IAS implementation, and thereafter. Implementation guidance should be developed for the industry, actuaries and auditors.

In short, insurers and the market need to be informed regarding the issues of IAS, or face a potentially damaging spiral of confusion and misunderstanding when IAS comes into force in 2005.

Chapter 6

Conclusion

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6.1 In summary

An ever-changing accounting environment faces South African companies, and long-term insurance companies in particular. This is substantially driven by a strategic decision to migrate South African accounting practice to international GAAP.

International Financial Reporting Standards (IFRS) are currently being updated with a view to the adoption of international GAAP in Europe and South Africa in 2005. This will require some changes for insurers in South Africa, most notably with regard to the disclosure and presentation requirements for insurance contracts and the layout and disclosure of the items in the income statement.

IFRS will transform the way analysts, investors and other key stakeholders assess value and performance. As mentioned before, there are some specific accounting issues relating to long-term insurance companies. These changes will impact on the reported results of long-term insurers.

This changing environment unfortunately leads to a lack of continuity or consistency in the reported results within the industry. In a period of transition, different companies respond to the changing standards according to their own individual circumstances.

At this stage the environment has not stabilised in the sense that new statements are still being issued and clear guidance on disclosure and presentation of items other than insurance contracts, is not yet available.

IFRS4 provides insurance companies with significant flexibility in how to apply the Phase I principles for the benefit of their company. This includes asset and liability designations and other techniques that may help to eliminate (or at least reduce) artificial volatility, along with disclosure practices that will help

organisations to explain strategies for promoting earnings stability and enhancing risk management.

Ultimately, each business is different and there can be no magic formula for responding in terms of IFRS. To succeed, insurers will need to evaluate the best options for their business as a central and early feature of their implementation strategy.

6.2 The withdrawal of AC121

The Accounting and Practices Board has taken a decision to align the text of statements of GAAP with that of International Financial Reporting Standards. The implication of this decision is that the South African Statements of GAAP will replicate IFRS. This means that over the next few months all statements of GAAP will be withdrawn and will be reissued. As a consequence it was proposed to withdraw AC121.

The South African Institute of Chartered Accountants' Long-term Insurance Interest Group met in early April 2004 to discuss the withdrawal of AC121 and its replacement by way of guidance. Eventually the Accounting Practices Committee firmly stated that they would not tolerate the ongoing implementation of AC121, as it contradicted a number of other statements and indeed overrode those statements. With this in mind, and taking into account the harmonisation program, they insisted that AC121 be withdrawn and be replaced by guidance notes only (Strachan, 2004b).

At the Long-term Insurance Interest Group meeting the draft guidance notes were approved and these have now been submitted to the APC, which has approved them. It would therefore appear as though any further work on the current insurance standard, AC121, falls away (Strachan, 2004b).

The withdrawal of AC121 can and will have far reaching implications for the long-term insurance industry in that there is no South African industry-specific guidance relating to the disclosure in the financial statements of long-term insurers.

6.3 Current challenges in the long-term insurance industry

As there is currently no plan to replace AC121, the current challenge in the long-term insurance industry is to present relevant, reliable and comparable financial statements. The current IAS trend is to provide less industry-specific statements and the rigid technical application of IAS can lead to non-comparable financial statements in the long-term insurance industry. Examples of this include:

- The effect of the withdrawal of AC121 is that the shareholders' and policyholders' interest in associated companies, subsidiary companies and joint ventures must be reflected at net asset value and not fair value as was the practice previously and that shares in holding companies held by policyholder funds, must be reflected at nil value and not fair value (Carstens, 2004).
- The application of IAS39 Financial instruments: Recognition and Measurement - Implementation Guidance and IAS18 Revenue on Investment contracts may give rise to reported losses on profitable contracts in year 1 and overstated profits in the years that follow (Olivier, 2004).
- The most recent proposed alterations to IAS39 Financial instruments: Recognition and Measurement - Implementation Guidance, might result in certain investment contract products and the underlying investments not being valued consistently. This might lead to temporary mismatching of assets and liabilities and will influence the reported earnings (Olivier, 2004).

It will be very important for long-term insurers to adequately disclose and explain the implications of these challenges in order to achieve comparability.

6.4 In conclusion

Investment analysts, shareholders, policyholders, auditors, standard setters and investors rely on the basic financial statement characteristic of comparability. The aim of the research was to assess the impact of the lack of authoritative South African financial reporting guidance relating to South African long-term insurers on the basic financial statement characteristic of **comparability**.

A literature study was undertaken and a checklist for disclosure in the long-term insurance industry was drawn up. The objective was to highlight areas of non-comparable disclosure for which financial reporting standards should be created in order to provide guidance on financial reporting by South African long-term insurers and, where possible, to suggest guidance.

Financial statements of selected South African long-term insurers were reviewed and “measured” against the checklist in order to make an assessment of comparability.

In view of the recent withdrawal of AC121 and the results of the comparability test in Chapter 4, there is reason to believe that each long-term insurer in South Africa discloses what it believes is right and what it believes the industry is required to disclose.

Currently the disclosure of industry-specific items differs significantly amongst long-term insurance companies in South Africa. The comparability test (on information disclosed in the 2002 annual reports of the selected companies) and the research done on industry-specific items identified by this test indicated the

extent of this non-comparability within the South African long-term insurance industry.

The author recommends that a long-term insurance industry accounting statement in the AC500 series should be issued, which should provide the appropriate guidance not only to preparers of financial statements, but also to other users of financial statements in the long-term insurance industry, until such time as the international accounting project relating to long-term insurers is complete. Some work will be required to update and/or amend a “new AC121” for the AC500 series.

6.5 Possibilities to extend this research

The Long-term Insurance Interest Group has launched projects to write new guidance notes that creates new research opportunities and new challenges for standard setters and preparers of financial statements of long-term insurers. Standards setters, users of the financial statements and the long-term insurance industry need to be cautious as to how quickly they move, relative to the withdrawal of AC121.

Considerable differences were found in the presentation and disclosure of selected items on the face of the income statements of the five selected insurers in the comparability test. Further research can be undertaken on the presentation of income statements of long-term insurers.

Further research can also be conducted on the disclosure and comparability of items in income statements and the related earnings on the face of the income statements of companies within the long-term insurance industry as well as the comparability of earnings disclosed by different industries.

A very interesting comparison, which also falls outside the scope of this research, will be insurance industry shareholder value as compared to other industries' shareholder value. The lack of comparability in disclosure results in a lack of shareholder value comparability within the long-term insurance industry and between the insurance industry and other sectors.

Negative Rand Reserves

If Negative Rand Reserves (NRR) were to be disallowed in financial instruments by IFRS, it would decrease the shareholder assets, but increase the value of in-force business. This would defer the emergence of profits and would also reduce the disclosed embedded value of the affected NRR (French, 2003).

Table 18 - Disclosure of Negative Rand Reserves

	SLM	OML	LIB	MOM	NAC
Disclosure of Negative Rand Reserves	x	x	x	x	x

Disclosure of NRRs is inadequate to estimate the potential impact of disallowing NRRs. Nobody is certain how this will influence financial reporting. However, if they were disallowed, earnings could be fairly severely impacted in the year of transition or an adjustment will have to be made against opening retained income.

It can be expected that the impact of the disallowance of second-tier margins and NRRs on the value of the shareholders' fund and the Value of In-Force respectively would offset one another to a certain extent from a disclosed embedded value point of view, although this may differ from company to company. The overall expectation is that the impact of the disallowance of NRRs will be more significant than that of the disallowance of second-tier margins (Nossel, *et al.*, 2003).

Further research can be conducted on NRRs as they have a potential impact on shareholder assets and the recognition of earnings reported by South African long-term insurers.

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Annual Reports

Old Mutual plc Annual Report, December 2002

Sanlam Limited Annual Report, December 2002

Liberty Group Limited Annual Report, December 2002

Firststrand Group Limited Annual Report, December 2002

New Africa Capital Annual Report, December 2002

Appendix A

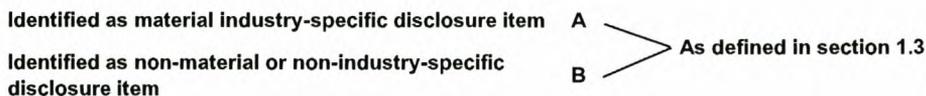
Results of the comparability test

Results of the comparability test

Key:

Sanlam Limited Annual Report 2002	SLM
Old Mutual plc Annual Report 2002	OML
Liberty Group Limited Annual Report 2002	LIB
Momentum Group Annual Report 2002	MOM
New Africa Capital Annual Report 2002	NAC
Classification as industry-specific (A) or non-industry-specific (B)	Class
Checklist was updated with items not included in the original checklist	Extra
Disclosed as required and comparable	✓
Disclosure not found or not comparable	x
Shown in other place in Annual Report	Other
Not applicable to the company	N/A
Author assumes it must be applicable to the company, but nothing disclosed	No information

Classification:



Key to classification of eight main elements for discussion in Chapter 4

- 4.2 The unique life fund and related earnings of a long-term insurer
 - 4.3 Premium income, policy benefits and outward reinsurance premiums or reinsurance recoveries
 - 4.4 Long-term Rate of Return (LTRR)
 - 4.5 Financial instruments and the implications for long-term insurance businesses
 - 4.6 Valuation issues
 - 4.7 Total assets under administration and total funds received from/paid to clients
 - 4.8 New business funds received
 - 4.9 Accounting for taxation and the deferred tax implications of capital gains tax in the long-term insurance industry
 - 6.5 Possibilities to extend this research
-

Income Statement		SLM 2002	OML 2002	LIB 2002	MOM 2002	NAC 2002	Class
	Note						
Income statement includes only items related to the shareholders' fund		✓	x	x	x	✓	A (4.3)
Income statement relates to both shareholders' and policyholders' funds		x	✓	✓	✓	x	A (4.3)
Income statement or notes disclose net income relating to shareholders and policyholders separately		✓	✓	✓	✓	✓	A (4.3)
FUNDS RECEIVED FROM CLIENTS	1	✓	✓	x	✓	✓	A (4.7)
Financial services income	2	✓	✓	✓	✓	✓	B
Outward reinsurance premiums		✓	✓	x	x	x	A (4.3)
Sales remuneration		✓	✓	✓	✓	✓	B
Income after sales remuneration							
Policy benefits	3	✓/x	✓	✓	✓	✓/x	A (4.3)
Administration costs	4	✓	✓	✓	✓	✓	B
Operating profit before tax	5	✓	✓	x	✓	✓	B
Tax on operating profit	6	✓	✓	✓	✓	✓	B
Operating profit from ordinary activities after tax		✓	✓	x	✓	✓	B
Minority shareholders' interest		✓	✓	N/A	✓	✓	B
Changes in other technical provisions, net of reinsurance							
Transfer to/from Policyholders' fund and Shareholders' fund		N/A	✓	✓	✓	N/A	A (4.2)
NET OPERATING PROFIT		✓	✓	x	x	✓	B
Net investment income							
Investment income	7	✓	✓	✓	✓	✓	B
Tax on investment income	6	✓	Other	Other	Other	Other	B
Minority shareholders' interest		✓	Other	Other	Other	Other	B
Net Equity accounted earnings	8						
Equity accounted earnings		✓	N/A	N/A	x	N/A	B
Tax on equity accounted earnings	6	✓	N/A	N/A	x	N/A	B
HEADLINE EARNINGS		✓	x	✓	✓	✓	B
Net investment surpluses (Investment surplus excluded from Headline Earnings)		✓	N/A	✓	x	x	A (4.5)
Amortisation of goodwill	16	✓	✓	✓	✓	✓	B
Dividends paid and proposed		Other	✓	Other	Other	Other	B
Foreign exchange movements		Other	✓	Other	Other	Other	B
ATTRIBUTABLE EARNINGS		✓	✓	✓	✓	✓	B
Diluted earnings per share:							
Net operating profit from ordinary activities	12	✓	Separate note for Earnings per share	x	Shown for Firststrand Limited (Holding Company)	x	B
Headline earnings	12	✓		✓		✓	B
Attributable earnings	12	✓		✓		✓	B
Dividend per share	13	✓	✓	✓		✓	B
PRO FORMA LTRR HEADLINE EARNINGS (R million)		✓	OML Headline Earnings are LTRR	x	x	x	A (4.4)
Pro forma LTRR headline earnings based on the long term rate of return (LTRR) (cents per share)		✓		x	x	x	A (4.4)

Group Balance Sheet

		SLM 2002	OML 2002	LIB 2002	MOM 2002	NAC 2002	Class
	Note						
ASSETS							
Non-current assets							
Fixed assets	14	✓	✓	✓	✓	✓	B
Owner-occupied properties	15	✓	x	✓	x	x	B
Goodwill	16	✓	✓	✓	x	x	B
Other intangible assets		N/A	N/A	✓	✓	✓	B
Investments	17	✓	✓	✓	✓	✓	B
Investment properties		✓	x	✓	✓	✓	B
Equities		✓	x	✓	✓	✓	B
Public sector stocks and loans		✓	x	✓	✓	✓	B
Debentures, insurance policies and other loans		✓	x	✓	✓	✓	B
Cash, deposits and similar securities		✓	x	✓	✓	✓	B
Deferred tax	18	✓	N/A	N/A	✓	✓	B
General reinsurance provisions	19	N/A	N/A	N/A	N/A	N/A	B
Current assets							
Trade and other receivables	20	✓	✓	✓	✓	✓	B
Cash, deposits and similar securities		✓	✓	✓	✓	✓	B
Deferred acquisition costs		(Note 1)	✓	(Note 1)	(Note 1)	(Note 1)	A (Note 2)
Present value of acquired in-force business		(Note 1)	✓	(Note 1)	(Note 1)	(Note 1)	A (Note 2)
Total assets		✓	✓	✓	✓	✓	B
EQUITY AND LIABILITIES							
Capital and reserves							
Share capital and premium	21	✓	✓	✓	✓	✓	B
Non-distributable reserves		✓	N/A	N/A	✓	✓	B
Merger reserve		N/A	✓	N/A	N/A	N/A	B
Equity component of convertible bonds		x	x	✓	x	x	B
Foreign currency translation reserve		x	x	x	x	✓	B
Retained income		✓	✓	✓	✓	✓	B
Shareholders' funds							
Minority shareholders' interest		✓	✓	✓	✓	✓	B
Non-current liabilities							
Long term policy liabilities	23	✓	✓	✓	✓	✓	A (4.2)
Other Long term liabilities	24	✓	✓	✓	✓	✓	B
Deferred tax	18	✓	N/A	✓	✓	✓	B
General insurance provisions	19	N/A	N/A	N/A	N/A	N/A	B
Current liabilities							
Trade and other payables	25	✓	✓	✓	✓	✓	B
Taxation		✓	✓	✓	✓	✓	B
Total equity and liabilities		✓	✓	✓	✓	✓	B
Segregated funds not included in the above balance sheet		✓	x	x	x	x	A (4.7)
Total assets under management and administration		✓	✓	x	x	x	A (4.7)
Tangible net asset value per share (cents)	28	✓	x	x	x	x	B
The Group balance sheet contains assets and liabilities of policyholders and shareholders, but discloses the total Policyholders' funds and Shareholders' funds separately							
		✓	✓	✓	✓	✓	A (4.2)
Separate information regarding the Shareholders' assets and liabilities is provided in addition to the policyholders' assets and liabilities (in either an additional balance sheet or in a note)							
		✓	x	✓	x	x	A (4.2)

Note 1: Not disclosed on Balance Sheet, but in the Embedded Value report or elsewhere.

Note 2: The information disclosed by OML is disclosed as per UK and the Association of British Insurers' requirements. South African long-term insurers disclose the same information as part of the Embedded Value report. This disclosure is discussed in 4.6 Valuation issues.

Statements of changes in Equity/Equity shareholder funds note

	Note	Share capital	Share premium	Investment reserve	Non-distributable reserve ⁽¹⁾	Retained income	Total
Balance at 1 January 2001		✓	✓	✓	✓	✓	✓
Attributable earnings for the year						✓	
Transfer to investment reserve	11			✓			
Dividends paid						✓	
Balance at 31 December 2001		✓	✓	✓	✓	✓	✓
Attributable earnings for the year						✓	
Transfer from investment reserve	11			✓			
Dividends paid						✓	
Cost of treasury shares acquired							
Balance at 31 December 2002		✓	✓	✓	✓	✓	✓

(1) Non-distributable reserve arising on acquisition of subsidiaries.

SLM	✓	✓	✓	✓	✓	✓	✓
OML	✓	✓	N/A	✓	✓	✓	✓
LIB	✓	✓	N/A	✓	✓	✓	✓
MOM	✓	✓	N/A	✓	✓	✓	✓
NAC	✓	✓	N/A	N/A	✓	✓	✓
Class	B	B	B	B	B	B	B

Group Cash Flow Statement

		SLM 2002	OML 2002	LIB 2002	MOM 2002	NAC 2002	Class
	Note						
Cash flow statement distinguishes between cash flows of shareholders' funds and policyholders' funds							
		✓	✓	x	x	x	A (4.2)
Net cash flow from operating activities							
		✓	✓	✓	✓	✓	B
Cash generated from operations before working capital	33.1	✓	✓	✓	✓	✓	B
Working capital changes		✓	✓	✓	✓	✓	B
Interest received/Interest paid		✓	✓	✓	✓	✓	B
Taxation		✓	✓	✓	✓	✓	B
Dividends received/Dividends paid		✓	✓	✓	✓	✓	B
Net cash flow from investment activities							
		✓	✓	✓	✓	✓	B
Net (acquisition)/disposal of investments		✓	✓	✓	✓	✓	B
Interest received/Taxation/Dividends received		✓	✓	✓	✓	✓	B
Rental income received		✓	✓	✓	✓	✓	B
Acquisition of subsidiaries	33.2	✓	✓	✓	✓	✓	B
Acquisition of treasury shares		✓	✓	✓	✓	✓	B
Net cash flow from financing activities							
Net term finance raised/(repaid), shares issued, InterCo		✓	✓	✓	✓	✓	B
Cash flow from movement in policyholders' funds							
		✓	✓	x	x	x	A (4.2)
Cash utilised in policyholders' activities	33.3	✓	x	x	x	x	A (4.2)
Taxation/Interest received/Dividends received	23.1	✓	x	x	x	x	A (4.2)
Other investment income	23.3	✓	x	x	x	x	A (4.2)
Net realised and unrealised investment surpluses	23.3	✓	x	x	x	x	A (4.2)
(Increase)/decrease in policyholders' investments		✓	x	x	x	x	A (4.2)
Increase/(decrease) in policy liabilities		✓	x	x	x	x	A (4.2)
Net increase in cash and cash equivalents							
		✓	✓	✓	✓	✓	B
Cash, deposits and similar securities at beginning of year		✓	✓	✓	✓	✓	B
Cash, deposits and similar securities at end of year		✓	✓	✓	✓	✓	B

BASIS OF PRESENTATION AND ACCOUNTING POLICIES

SLM	OML	LIB	MOM	NAC	Class
A. BASIS OF PRESENTATION					
<p>POLICYHOLDERS' AND SHAREHOLDERS' ACTIVITIES</p> <p>The assets, liabilities and activities of the policyholders and shareholders in respect of the life insurance business are managed separately and are governed by the valuation bases for policy liabilities and profit entitlement rules which are determined in accordance with prevailing legislation, generally accepted actuarial practice and the stipulations contained in the demutualisation proposal. The valuation bases in respect of policy liabilities and profit entitlement of shareholders are set out on pages X to X.</p> <p>The group financial statements set out on pages X to X include the consolidated activities of the policyholders and shareholders. Separate financial information on the activities of the shareholders of the Sanlam Limited group is disclosed on pages X to X. The Statement of Actuarial Values of Assets and Liabilities of the life insurance business of the Group is disclosed on pages X to X.</p>	<p>UK GAAP</p> <p>Sharper focus on life assurance and banking disclosed separately.</p>	✓	✓	✓, except profit entitlement not disclosed.	A (4.2)
	Complies with Statement of Recommended Practice issued by the Association of British Insurers ("ABI SORP")	✓	✓	✓	A (4.2)
<p>ACTUARIAL VALUES OF ASSETS AND LIABILITIES</p> <p>The actuarial values of assets and liabilities are the consolidated financial position of the xxxxx Life Insurance Limited group, excluding xxxxxxxxxxxxxx and xxxxxxxxxxxxxx, which are included at fair value as determined by the Board of Directors. Associated companies are treated as investments and are not equity accounted for.</p>	✓	✓, except as noted below: The life funds include deferred tax on unrealised capital gains in respect of Policyholder investments.	✓	✓	A (4.6)
<p>FUNDS RECEIVED FROM CLIENTS</p> <p>Funds received from clients consist of single and recurring long term and general insurance premium income, which are included in the financial statements, as well as unit trust contributions, inflow for assets managed and administered on behalf of clients and non-life insurance linked-product contributions, which are not included in the financial statements as they are funds held on behalf of and at the risk of clients. Transfers between the various types of business, other than those transacted at arm's length, are eliminated.</p>	X	X	X	X	A (4.7)
<p>NEW BUSINESS</p> <p>In the case of long term insurance business the value of all new policies that have incepted during the financial year and have received at least one premium is regarded as new business.</p> <p>All segregated funds inflows, unit trust inflows and general insurance premiums are regarded as new business.</p>	X	X	X	X	A (4.8)
	X	X	X	X	A (4.8)

SLM

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Class

	OML	LIB	MOM	NAC	Class
<p>FINANCIAL SERVICES INCOME</p> <p>Financial services income for the shareholders consists of:</p> <ul style="list-style-type: none"> · income earned from long term insurance activities such as investment and administration fees, risk underwriting premiums, asset mismatch profits or losses and income earned on working capital; · income from general insurance business, including income earned on working capital; · income from banking activities such as realised and unrealised gains or losses on trading accounts, unsecured corporate bonds and money market assets and liabilities, other securities related income and fees, and commissions; · income from other financial services such as unit trust administration, trust services and linked-product business. 	X	X	X	X	B
<p>SEGREGATED FUNDS</p> <p>Sanlam also manages and administers assets for the account of and at the risk of clients. As these are not the assets of the Sanlam group, they are not reflected in the Sanlam group balance sheet but are disclosed in a footnote to the balance sheet.</p>	X	X	X	X	A (4.7)
<p>OTHER LONG TERM LIABILITIES</p> <p>The portion which is repayable within one year is not transferred to current liabilities. This is consistent with the treatment of investments redeemable within one year that are not included in current assets.</p>	✓	✓	✓	✓	B

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Class

B. ACCOUNTING POLICIES					
<p>The group financial statements are prepared applying the principal accounting policies below, which are in accordance with and comply with South African Statements of Generally Accepted Accounting Practice, and some of which apply specifically to the life insurance industry.</p>	<p>X (UK based)</p>	<p>✓</p>	<p>✓</p>	<p>✓</p>	<p>B</p>
<p>BASIS OF CONSOLIDATION According to AC132 and AC131.</p> <p>Where shares in group companies are held as investments for policyholder benefits they are not eliminated on consolidation but reflected at fair value as equity investments in the balance sheet.</p> <p>In certain instances, a portion of the Sanlam group's interest in consolidated subsidiaries is held by the policyholders' fund to fund future benefits in terms of its policyholders' contracts. The excess of the fair value of the policyholders' interest in these consolidated subsidiaries over their proportionate share of the subsidiaries' net assets is recognised in the group balance sheet as equity investments.</p>	<p>Done according to AC132 and AC131, except for investment management fees charged by Group asset management companies to long-term business funds.</p> <p>In accordance with the ABI SORP, policyholder liabilities of the Group's US life subsidiaries are incorporated into the Group's accounts on a US GAAP basis. Investment accounting is according to UK GAAP.</p>	<p>✓</p> <p>X</p>	<p>✓</p> <p>X</p>	<p>✓</p> <p>X</p>	<p>B</p> <p>B</p>
<p>ASSOCIATED COMPANIES According to AC110</p> <p>The results of associated companies have been accounted for using the equity method of accounting, where the Group's share of the associated companies earnings before dividends is included in earnings. Where the associate is held as an investment, the equity-accounted earnings are included in investment income with a corresponding adjustment to the carrying value of the investment in associated companies. This carrying value is adjusted to fair value with a corresponding adjustment to investment surpluses on the investment in associated companies in the income statement.</p>	<p>N/A</p>	<p>N/A</p>	<p>✓</p>	<p>N/A</p>	<p>B</p>
<p>JOINT VENTURES According to AC119</p>	<p>N/A</p>	<p>✓</p>	<p>N/A</p>	<p>N/A</p>	<p>B</p>
<p>GOODWILL According to AC131. Where applicable, goodwill is translated to South African rand using historical rates.</p>	<p>✓</p>	<p>✓</p>	<p>✓</p>	<p>✓</p>	<p>B</p>

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Class

<p>INTANGIBLE ASSETS No value is attributed to internally developed trademarks or similar rights and assets. Costs incurred on these items, whether purchased or created by the Group, are charged to the income statement in the period in which they are incurred.</p>	<p>✓</p>	<p>X Computer software development costs are capitalised</p>	<p>X Computer software development costs and Prepaid contracts (health insurance) are capitalised</p>	<p>X Computer software development costs and Prepaid contracts (health insurance) are capitalised</p>	<p>B</p>
<p>FINANCIAL INSTRUMENTS Financial instruments carried on the balance sheet include cash and bank balances, investments, receivables and trade creditors. These instruments are generally carried at their fair value. The particular recognition methods adopted are disclosed in the individual policy statements associated with each item.</p>	<p>N/A</p>	<p>✓</p>	<p>✓</p>	<p>✓</p>	<p>B</p>
<p>INVESTMENT PROPERTIES/PROPERTIES UNDER DEVELOPMENT Detail as to the measurement/gains and losses N/A</p>	<p>N/A</p>	<p>✓</p>	<p>N/A</p>	<p>✓</p>	<p>B</p>
<p>INVESTMENTS Investments are reflected at fair value, which has been determined on the following bases: a) The value of fixed properties, which generates income, is determined by discounting expected future cash flows at appropriate market interest rates. Other fixed property is valued at cost less provision for impairment in value, where appropriate; b) Listed shares and units in unit trusts are valued at the stock exchange and repurchase prices respectively. The value of unlisted shares is determined by the directors using appropriate valuation bases; c) Interest-bearing investments are valued by discounting expected future cash flows at appropriate market interest rates; d) Listed bonds are valued at the stock exchange prices; e) Listed derivative instruments are valued at the South African Futures Exchange prices and the value of unlisted derivatives is determined by the directors using generally accepted valuation models;</p>	<p>✓ Different GAAP requirements (UK GAAP)</p>	<p>✓ ✓ ✓ ✓ ✓ ✓</p>	<p>✓ ✓ ✓ ✓ ✓ X</p>	<p>✓ ✓ ✓ ✓ ✓ ✓</p>	<p>B B B B B B</p>
<p>DERIVATIVE INSTRUMENTS According to AC125 and AC133. Non-trading transactions are those which are held for hedging purposes as part of the Group's risk management strategy against assets, liabilities, positions or cash flows measured at fair value as well as structures incorporated in the product design of policyholder products. Gains and losses on derivative financial instruments incorporated in policyholder products are included in policy liabilities.</p>	<p>✓ Different GAAP requirements (UK GAAP)</p>	<p>✓</p>	<p>✓</p>	<p>✓</p>	<p>A (4.5)</p>

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<p>FOREIGN CURRENCY TRANSLATION RESERVE According to AC132 and AC 112. A negative foreign currency translation reserve will not be created.</p>	<p>✓ ✓</p>	<p>✓ ✓</p>	<p>✓ ✓</p>	<p>✓ ✓</p>	<p>B B</p>
<p>INVESTMENT RESERVE Net realised and unrealised investment surpluses on the revaluation or sale of investments attributable to shareholders are transferred to an investment reserve. However, the Board may transfer realised investment surpluses to retained income. A negative investment reserve will not be created. Realised and unrealised investment surpluses attributable to policyholders are included in policy liabilities.</p>	<p>N/A</p>	<p>N/A</p>	<p>✓</p>	<p>N/A</p>	<p>B</p>
<p>PROVISIONS AC 130</p>	<p>✓</p>	<p>✓</p>	<p>✓</p>	<p>✓</p>	<p>B</p>
<p>FIXED ASSETS AC 123. SLM is very unclear and vague about their fixed assets. Depreciation write-off periods disclosed vary from anything between two and twenty years and no exact write-off period per asset class is disclosed.</p>	<p>✓ More complete information about types of assets and write-off periods than SLM, but still not clear information on the exact write-off periods.</p>	<p>✓ More complete information about types of assets and write-off periods than SLM, but still not clear information on the exact write-off periods.</p>	<p>✓ More complete information about types of assets and write-off periods than SLM, very clear information on the exact write-off periods.</p>	<p>✓ More complete information about types of assets and write-off periods than SLM, but still not clear information on the exact write-off periods.</p>	<p>B</p>
<p>SCRIP LENDING Scrip lending fees are included in Income statement as investment income. Are split between Policyholders funds and Shareholders funds.</p>	<p>X</p>	<p>✓</p>	<p>✓</p>	<p>✓</p>	<p>B</p>
<p>LEASES AC 105</p>	<p>N/A</p>	<p>✓</p>	<p>✓</p>	<p>N/A</p>	<p>B</p>
<p>INVESTMENT RETURN Investment income AC 111. Investment income earned on working capital is included in operating profit. Investment surpluses AC 133. These surpluses are recognised in the income statement or policy liabilities on the date of sale or on the date of valuation to fair value.</p>	<p>AC 111 and AC133 (like SLM). OML discloses policy of split between Policyholders funds and Shareholders funds investment return as based on LTRR.</p>	<p>✓ X X</p>	<p>✓ X X</p>	<p>✓ X X</p>	<p>B B A (4.2)</p>

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Class

<p>LONG TERM RATE OF RETURN The long term rate of return (LTRR) is determined at the beginning of the year by the directors and is primarily based on the actuarial assumptions, taking into account historical experience and current market conditions having regard to inflation expectations and consensus economic and investment forecasts. The directors have selected this rate with a view to ensuring that investment returns credited to LTRR headline earnings are consistent with the actual returns expected to be earned over the long term.</p> <p>The long term investment return is calculated on a monthly basis on the fair value of the investments held in the shareholders' funds and holdings in subsidiaries and associated companies.</p>	<p>X</p>	<p>X</p>	<p>X</p>	<p>X</p>	<p>A (4.4)</p>
<p>PREMIUM INCOME The full annual premiums on individual insurance policies that are receivable in terms of the policy contracts are accounted for on policy anniversary dates, notwithstanding that premiums are payable in instalments. The monthly premiums in respect of certain new products are in terms of their policy contracts accounted for when due.</p> <p>Group life insurance premiums are accounted for when receivable. Where premiums are not determined in advance they are accounted for upon receipt.</p> <p>Gross premium income is reduced by reinsurance premiums applicable to the same period.</p> <p>Reinsurance premiums/recoveries disclosed</p>	<p>✓ X ✓ ✓</p>	<p>✓ ✓ ✓ X</p>	<p>✓ ✓ ✓ X</p>	<p>✓ ✓ ✓ X</p>	<p>A (4.3) A (4.3) A (4.3) A (4.3)</p>
<p>CONSULTING FEES EARNED Consulting fees are accounted for on the accrual basis.</p>	<p>✓</p>	<p>N/A</p>	<p>N/A</p>	<p>N/A</p>	<p>B</p>
<p>POLICY BENEFITS Policy claims received up to the last day of each financial period.</p> <p>Disclose IBNR</p> <p>Policy benefits are reflected net of amounts recovered from reinsurers.</p> <p>Outstanding claims/benefits stated net of reinsurance X</p>	<p>✓ X X ✓</p>	<p>✓ X ✓ ✓</p>	<p>✓ X ✓ X</p>	<p>✓ X ✓ X</p>	<p>A (4.3) A (4.6) A (4.3) A (4.3)</p>
<p>SALES REMUNERATION AC 000. Commission on long term insurance business is accounted for in the financial period during which it is incurred.</p>	<p>Acquisition costs on the Balance Sheet.</p>	<p>✓ - As OML</p>	<p>✓ - As SLM</p>	<p>✓ - As SLM</p>	<p>B</p>
<p>NEW BUSINESS COSTS New business costs are recognised in the Income Statement when incurred and forms part of the Actuarial liabilities in accordance with Actuarial Standards (GAAS) X</p>	<p>X</p>	<p>✓</p>	<p>X</p>	<p>X</p>	<p>A (4.8)</p>

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ADMINISTRATION COSTS AC 000.	✓	✓	✓	✓	B
TAXATION SA Life insurance - four-fund method x	X	X	✓	X	A (4.9)
DEFERRED INCOME TAX AC 102. Deferred capital gains tax relating to the assets underlying the policyholders' funds is included in policy liabilities.	✓	✓	✓	✓	A (4.9)
FOREIGN CURRENCIES Transactions and balances AC 112	OML discloses the currency and the rates used.	✓	✓	✓	B
Foreign entities AC 112		✓	✓	✓	B
Foreign operations AC 112		✓	✓	✓	B
RETIREMENT BENEFITS		✓	✓	✓	✓
Defined benefit plans AC 116	No info or N/A	No info or N/A	✓	✓	B
Defined contribution plans AC 116	No info or N/A	No info or N/A	✓	✓	B
Medical aid benefits AC 116	x	✓	x	x	B
Post-retirement medical aid benefits AC 116	x	x	✓	✓	B
EQUITY COMPENSATION PLANS xxxxx operates a staff share incentive scheme through xxxxxx Limited Share Incentive Trust. Shares are offered on a combined option and deferred delivery basis, which staff can take up in tranches over a period of up to six years. The beneficiaries under the scheme are executive directors, management and sales advisors employed on a full time basis. There is currently no income statement effect when such benefits are granted.	✓	✓	N/A	N/A	B

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Class

<p>SEGMENTAL REPORTING AC 115</p>	<p>x</p>	<p>✓</p>	<p>✓</p>	<p>✓</p>	<p>B</p>
<p>DIVIDENDS Dividends proposed or declared after the balance sheet date are not recognised at the balance sheet date.</p>	<p>✓</p>	<p>✓</p>	<p>✓</p>	<p>✓</p>	<p>B</p>
<p>BORROWING COSTS Borrowing costs are capitalised up and till the date the construction or installation is complete.</p>	<p>N/A</p>	<p>N/A</p>	<p>✓</p>	<p>N/A</p>	<p>B</p>
<p>RELATED PARTIES x</p>	<p>x</p>	<p>x</p>	<p>✓</p>	<p>x</p>	<p>B</p>

SLM

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Class

SLM	OML	LIB	MOM	NAC	Class
C. Policy liabilities and profit entitlement					
Valuation in accordance with PGN 104 of the Actuarial Society of South Africa	✓	✓	✓	✓	A (4.2)
Second-tier margins are included	✓	✓	✓	✓	A (4.2)
Separate group and individual business	✓	x	✓	✓	A (4.2)
HIV/Aids reserve	✓	x	✓	✓	A (4.2)
Reduction in earnings caused by using a retrospective HIV/Aids valuation basis instead of a prospective valuation basis	✓	x	x	x	A (4.2)
Asset mismatch reserve	✓	x	x	x	A (4.6)
Deferred capital gains tax	✓	x	✓	✓	A (4.9)
Information on basic product types included	✓	x	x	x	A (4.2)
Disclosure of Negative Rand Reserves	x	x	x	x	A (6.5)
Disclosure of bonus stabilisation reserves	✓	x	x	x	A (4.2)
Linked and market related business:					
Liability equals the market value of underlying assets	✓	✓	✓	✓	A (4.6)
Adjusted to allow for the discounted present value of the difference between expected future expenses and charges	✓	No information disclosed	✓	✓	A (4.6)
Stable/smoothed bonus business:					
Liability equals the sum of accumulated investment accounts (i.e. market value or underlying assets) less the present value of future charges not required for risk benefits and expenses	✓	No information disclosed	✓	✓	A (4.6)
A bonus stabilisation reserve is kept	✓	✓	✓	✓	A (4.2)
Non-participating (conventional) business:					
Liability valued prospectively	x	x	✓	✓	A (4.6)
Liability valued retrospectively	✓	✓	x	x	A (4.6)
Annuities:					
Liability equals the present value of expected benefit payments and expenses less present value of expected future premium receipts	✓	✓	✓	✓	A (4.6)
Guaranteed plans:					
Liability equals the discounted maturity values and expected future expenses	✓	✓	No information disclosed	✓	No information disclosed
Profit entitlement policies					
General reference to profit entitlement policies	✓	✓	✓	✓	x
More detail on profit entitlement policies	✓	x	✓	✓	x
Embedded value/Achieved profits					
Audited report	✓	✓	✓	✓	A (4.6)
Basis of preparation disclosed	✓	✓	✓	✓	A (4.6)
Detail of embedded value earnings provided	✓	✓	✓	✓	A (4.6)
Assumptions provided (valuation assumptions and discount rates)	✓	✓	✓	✓	A (4.6)
Sensitivity analysis on value of in-force business	✓	✓	✓	✓	A (4.6)
Sensitivity analysis on value of new business	✓	✓	✓	✓	A (4.6)
Capital adequacy requirements (CAR)					
CAR and CAR multiple provided	✓	✓	✓	✓	A (4.6)
Details of assumptions	✓	x	✓	✓	A (4.6)
Management actions disclosed	✓	x	✓	✓	A (4.6)
Note: As Old Mutual's primary listing is in the United Kingdom, it adhered to the Association of British Insurers' (ABI) guidance on disclosing information on "achieved profits" in its 2002 Annual Report. This replaces the embedded value information provided in previous years. (Old Mutual plc. Annual Report, 2002: 12)					

Notes to the Group financial statements

	SLM 2002	OML 2002	LIB 2002	MOM 2002	NAC 2002	Class
1. FUNDS RECEIVED FROM CLIENTS						
Insurance business - Premium income	✓	✓	✓	✓	✓	A (4.7)
Long term insurance (note 23.2)	✓	X	X	✓	X	A (4.7)
Transfer to segregated funds	✓	X	X	X	X	A (4.7)
General insurance	✓	X	X	X	X	B
Other business						
Unit trusts	✓	X	X	X	X	B
Linked products	✓	X	X	X	X	A (4.7)
Segregated funds	✓	X	X	X	X	A (4.7)
Health Care	✓	X	X	✓	X	B
Total funds received from clients	✓	✓	X	✓	✓	A (4.7)
Premium income shown net of reinsurance premiums	✓	X	✓	✓	✓	A (4.3)
2. FINANCIAL SERVICES INCOME						
Long term insurance	✓	X	X	X	✓	A (4.3)
General insurance	✓	X	X	X	✓	B
Other financial services	✓	X	X	X	✓	B
Total financial services income	✓	✓	X	X	✓	B
Included in financial services income is						
Dividend income	✓	X	X	X	✓	B
Interest received	✓	X	X	X	✓	B
Interest paid and term finance costs	✓	X	X	X	✓	B
3. POLICY BENEFITS (Note relates to Income statement disclosure. See also note 26)						
Underwriting policy benefits	✓	X	X	X	✓	A (4.3)
Total claims & policyholder benefits	X	✓	✓	✓	X	A (4.3)
Total policy benefits paid in Income statement (Policyholder and Shareholder payments)	X	✓	✓	✓	X	A (4.3)
Policyholder benefit payments net of reinsurance recoveries	✓	X	✓	✓	✓	A (4.3)
4. ADMINISTRATION COSTS						
Details of administration costs	✓	✓	✓	✓	✓	B
5. ANALYSIS OF OPERATING PROFIT						
Total operating profit per business segment	✓	✓	✓	✓	✓	B
Total operating profit per geographical segment	✓	Not for life business	X	X	✓	B

Notes to the Group financial statements

SLM 2002	OML 2002	LIB 2002	MOM 2002	NAC 2002	Class
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6. TAXATION: SHAREHOLDERS' funds
Analysis of income tax on earnings of shareholders' funds
Operating profit

current year	✓	x	x	✓	x	B
prior year	✓	x	x	✓	x	B

Investment income

current year	✓	x	x	✓	x	B
prior year	✓	x	x	✓	x	B

Equity accounted earnings

current year	✓	N/A	N/A	x	N/A	B
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Investment surpluses

Net investment surpluses - normal	✓	x	x	x	x	B
- capital gains tax	✓	x	x	x	x	B
Investment surplus on investment in associated company	✓	N/A	N/A	x	N/A	B
- capital gains tax	✓	N/A	N/A	x	N/A	B

Income tax on earnings

current year	✓	✓	✓	✓	✓	B
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Income tax

Normal income tax	✓	✓	✓	✓	✓	B
RSA – current year	✓	✓	✓	✓	✓	B
Foreign	✓	✓	✓	✓	✓	B
Capital gains tax	✓	✓	✓	✓	✓	B
Deferred tax	✓	✓	✓	✓	✓	B
Normal tax - current year	✓	✓	✓	✓	✓	B
- prior year	✓	✓	✓	✓	✓	B
Capital gains tax	✓	x	✓	✓	✓	B
Share of associate companies' tax charge	✓	N/A	N/A	x	N/A	B
Taxation	✓	✓	✓	✓	✓	B

6. TAXATION: SHAREHOLDERS' FUNDS
Reconciliation of tax rate on operating profit

Standard rate of taxation	✓	✓	✓	x	✓	B
Adjusted for:						
Non-taxable income	✓	✓	✓	x	✓	B
Prior year adjustments	✓	✓	✓	x	✓	B
Foreign tax rate differential	✓	✓	✓	x	✓	B
Other	✓	✓	✓	x	✓	B
Effective tax rate on operating profit	✓	✓	✓	x	✓	B

Reconciliation of tax rate on investment return

Standard rate of taxation	✓	x	x	x	x	B
Adjusted for:						
Non-taxable income	✓	x	x	x	x	B
Investment surpluses	✓	x	x	x	x	B
Prior year adjustments	✓	x	x	x	x	B
Equity accounted earnings	✓	N/A	N/A	x	N/A	B
Other	✓	x	x	x	x	B
Effective tax rate on investment return	✓	x	x	x	x	B

7. INVESTMENT RETURN: SHAREHOLDERS' FUNDS
Investment income - (included in Financial services income for SLM)

Interest-bearing investments	✓	✓	✓	✓	✓	B
Equities	✓	✓	✓	✓	✓	B
Properties	✓	✓	✓	✓	✓	B

Investment surpluses

Realised and unrealised investment surpluses	✓	x	✓	x	✓	B
(Deficit)/surplus on investment in associate company	✓	N/A	N/A	x	N/A	B
Change in accounting policy by subsidiary	✓	N/A	✓	N/A	✓	B

Investment return: shareholders' funds

current year	✓	✓	✓	✓	✓	B
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8. NET EQUITY-ACCOUNTED EARNINGS

Investment surplus and dividends received on investment in associate	✓	N/A	N/A	✓	N/A	B
Less : Balance over equity accounted earnings transferred (from)/to net	✓	N/A	N/A	x	N/A	B
Investment surplus	✓	N/A	N/A	x	N/A	B
Capital gains tax	✓	N/A	N/A	x	N/A	B

Net equity-accounted earnings

current year	✓	N/A	N/A	✓	N/A	B
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Notes to the Group financial statements

	SLM 2002	OML 2002	LIB 2002	MOM 2002	NAC 2002	Class
9. PRO FORMA LONG TERM RATE OF RETURN HEADLINE EARNINGS						
Long term rate of return (LTRR) headline earnings						
Net operating profit	✓	✓	X	X	X	A (4.4)
LTRR Investment return						
Net equity accounted earnings	✓	✓	X	X	X	A (4.4)
Investment return after taxation	✓	✓	X	X	X	A (4.4)
LTRR headline earnings	✓	✓	X	X	X	A (4.4)
Reconciliation of headline earnings and LTRR headline earnings						
Headline earnings per income statement	✓	X	X	X	X	A (4.4)
Net investment surpluses	✓	X	X	X	X	A (4.4)
Net LTRR adjustment	✓	X	X	X	X	A (4.4)
LTRR headline earnings	✓	X	X	X	X	A (4.4)
Analysis of net LTRR adjustment						
Investment return	✓	X	X	X	X	A (4.4)
Equities	✓	X	X	X	X	A (4.4)
Deficit/(surplus) on investment in associate company	✓	N/A	N/A	X	N/A	A (4.4)
Interest bearing investments	✓	X	X	X	X	A (4.4)
Properties	✓	X	X	X	X	A (4.4)
Tax	✓	X	X	X	X	A (4.4)
Minority shareholders' interest	✓	X	X	X	X	A (4.4)
Net LTRR adjustment	✓	X	X	X	X	A (4.4)
A comparison of the aggregate actual and calculated longer term returns (after tax and minorities) since xxxxxx is set out below						
Actual returns	✓	✓	X	X	X	A (4.4)
Longer term returns	✓	✓	X	X	X	A (4.4)
(Deficit)/excess aggregate short term fluctuations	✓	✓	X	X	X	A (4.4)
A reconciliation of the investments included in the calculation of the LTRR is as follows:						
Investments per shareholders' funds balance sheet	✓	X	X	X	X	A (4.4)
Less: Investment in associated company	✓	N/A	N/A	X	N/A	A (4.4)
Investments held in respect of term finance	✓	X	X	X	X	A (4.4)
Investments held in respect of banking activities	✓	X	X	X	X	A (4.4)
Non-cash free float assets of subsidiary	✓	X	X	X	X	A (4.4)
Other	✓	X	X	X	X	A (4.4)
LTRR investments	✓	X	X	X	X	A (4.4)
Analysis of LTRR investments						
Equities	✓	X	X	X	X	A (4.4)
Securities	✓	X	X	X	X	A (4.4)
Cash, deposits and similar securities	✓	X	X	X	X	A (4.4)
Properties	✓	X	X	X	X	A (4.4)
LTRR investments	✓	X	X	X	X	A (4.4)

Notes to the Group financial statements

	SLM 2002	OML 2002	LIB 2002	MOM 2002	NAC 2002	Class
11. TRANSFER (FROM)/TO INVESTMENT RESERVE						
Net investment surpluses (note 7)	✓	N/A	x	N/A	x	B
Tax on net investment surpluses (note 6)	✓	N/A	x	N/A	x	B
Minority interest in net investment surpluses	✓	N/A	x	N/A	x	B
Change in accounting policy by subsidiary (note 7)	✓	N/A	x	N/A	x	B
Negative reserve transferred to retained income	✓	N/A	x	N/A	x	B
Transfer (from)/to investment reserve	✓	N/A	x	N/A	x	B
Similar to the transfer of a negative investment reserve to retained earnings, a negative foreign currency reserve is not created. At year end a negative currency reserve is kept in retained earnings.	✓	N/A	x	N/A	x	B
12. DILUTED EARNINGS PER SHARE						
For diluted earnings per share the weighted average number of ordinary shares is adjusted for the shares not yet issued under the Share Incentive Scheme as well as treasury shares held by subsidiaries. Diluted earnings per share is calculated by dividing earnings by the adjusted weighted average number of shares in issue.	✓	A full recon. of Earnings is given.	If no dilutive factors - N/A	If no dilutive factors - N/A	If no dilutive factors - N/A	B
Net operating profit from ordinary activities	✓	✓	x		✓	B
Headline earnings	✓	x	✓		✓	B
Headline earnings based on the long term rate of return	✓	✓	x	Disclosed by Firststrand Ltd	x	B
Attributable earnings	✓	✓	✓		✓	B
Number of ordinary shares in issue	✓	✓	✓		✓	B
Recon of adjusted weighted average number of shares	✓	✓	✓		x	B
Disclosure of diluted earnings per share						
Net operating profit from ordinary activities	✓	✓	x		✓	B
Headline earnings	✓	x	✓	Disclosed by Firststrand Ltd	✓	B
Headline earnings based on the long term rate of return	✓	✓	x		x	B
Attributable earnings	✓	✓	✓		x	B
13. DIVIDENDS						
A dividend of ___ cents per share (2001: cents per share) was declared.	✓	✓	✓	✓	✓	B
14. FIXED ASSETS						
Land and buildings	✓	✓	✓	✓	✓	B
Computer equipment	✓	✓	✓	✓	✓	B
Cost	✓	✓	✓	✓	✓	B
Accumulated depreciation	✓	✓	✓	✓	✓	B
Furniture, equipment and vehicles	✓	✓	✓	✓	✓	B
Cost	✓	✓	✓	✓	✓	B
Accumulated depreciation	✓	✓	✓	✓	✓	B
Total fixed assets	✓	✓	✓	✓	✓	B
The reconciliation of the movement in the book value of fixed assets is not provided, as it is not considered material in relation to the Groups' activities.	x	Full recon. disclosed	Full recon. disclosed	Full recon. disclosed	Full recon. disclosed	B
15. OWNER-OCCUPIED PROPERTIES						
Balance at beginning of year	✓	N/A	✓	N/A	N/A	B
Transfer from fixed assets at depreciated value	✓	N/A	✓	N/A	N/A	B
Transfer from investment properties at fair value	✓	N/A	✓	N/A	N/A	B
Net expenditure expensed	✓	N/A	✓	N/A	N/A	B
Balance at end of year	✓	N/A	✓	N/A	N/A	B
Depreciation is provided for over the useful life of owner-occupied properties, taking into account an expected residual value. If the expected residual value is equal to or greater than the carrying value, no depreciation is provided for.	✓	N/A	✓	N/A	N/A	B
16. GOODWILL						
Balance at beginning of year	✓	✓	✓	N/A	N/A	B
Additions during the year						
Net consideration paid	✓	✓	✓	N/A	N/A	B
Fair value of net assets acquired	✓	✓	✓	N/A	N/A	B
Amortisations	✓	✓	✓	N/A	N/A	B
Balance at end of year	✓	✓	✓	N/A	N/A	B
Full description on reasons and background for goodwill adjustments. Analysis of goodwill between Life, AM, Bank, General ins.	x	✓	x	N/A	N/A	B
OTHER INTANGIBLE ASSETS						
Computer software internally generated	x	x	✓	✓	✓	B

Notes to the Group financial statements	SLM 2002	OML 2002	LIB 2002	MOM 2002	NAC 2002	Class
17. INVESTMENTS						
Spread of investments in equities listed on JSE by sector						
Industrial	✓	✓	✓	✓	✓	B
Financial	✓	✓	✓	✓	✓	B
Resources	✓	✓	✓	✓	✓	B
EXTRA: LIB, MOM and NAC provide full note disclosure on investment properties. Classification of investment properties: Completed, under development, office buildings, shopping malls, hotels, vacant land, industrial.						
	X	X	✓	✓	✓	B
Unlisted equity investments						
As a percentage of the total investment in equities	✓	X	✓	✓	✓	B
Direct offshore investments						
Equities	✓	X	✓	X	✓	B
Interest-bearing investments	✓	X	✓	X	✓	B
Total offshore investments	✓	X	✓	X	✓	B
Shares held in holding company						
Holding company shares held by policyholders' funds						
Number	✓	✓	X	X	X	A (Note1)
Fair value	✓	✓	X	X	X	A (Note1)
Investment in associated companies						
Fair value of interest	✓	N/A	N/A	✓	N/A	B
Number of shares held	✓	N/A	N/A	✓	N/A	B
Interest in issued share capital						
Shareholders' funds	✓	N/A	N/A	✓	N/A	A (Note1)
Policyholders' funds	✓	N/A	N/A	✓	N/A	A (Note1)
Share of earnings after tax for current year						
Shareholders' funds	✓	N/A	N/A	✓	N/A	A (Note1)
Policyholders' funds	✓	N/A	N/A	✓	N/A	A (Note1)
Distributions received						
Shareholders' funds	✓	N/A	N/A	✓	N/A	A (Note1)
Policyholders' funds	✓	N/A	N/A	✓	N/A	A (Note1)
Aggregate post-acquisition reserves attributable to shareholders	✓	N/A	N/A	✓	N/A	B
Investment in joint venture						
Details/background	✓	N/A	✓	N/A	N/A	B
Carrying value of interest	✓	N/A	✓	N/A	N/A	B
Share of earnings after tax	✓	N/A	✓	N/A	N/A	B
Share of aggregate assets	✓	N/A	✓	N/A	N/A	B
Share of aggregate liabilities	✓	N/A	✓	N/A	N/A	B
Register of investments						
A register containing details of all investments, including fixed property investments, is available for inspection at the registered office of the holding company.						
	✓	X	X	✓	✓	B
Detailed information on acquisitions and disposals, terms, fair value, performance.						
	X	✓	✓	X	X	B
Derivative assets (Interest bearing and Equity split)						
	X	X	X	✓	X	B

Note 1: Although the items disclosed are industry-specific, they were not regarded as material. The unique separation between policyholders and shareholders is discussed in section 4.1. The disclosure of who holds the shares in associated companies is not material to the users of long-term insurance financial statements.

Notes to the Group financial statements

	SLM 2002	OML 2002	LIB 2002	MOM 2002	NAC 2002	Class
18. DEFERRED TAX AND PROVISIONS						
Details of the deferred tax balances and provisions are as follows:	Provisions and Deferred Tax Asset/Liab.	Provisions and Deferred Tax Asset/Liab.	Provisions and Deferred Tax Asset/Liab.	Provisions and Deferred Tax Asset/Liab.	Provisions and Deferred Tax Asset/Liab.	
Balance at 1 January 2002						
Charged to income statement	✓	✓	✓	✓	✓	B
Additional provisions - normal	✓	✓	✓	✓	✓	B
Additional provisions - capital gains tax	✓	✓	✓	✓	✓	B
Unused amounts reversed	✓	✓	✓	✓	✓	B
Prior year adjustment by subsidiary	✓	✓	✓	✓	✓	B
Utilised during the year	✓	✓	✓	✓	✓	B
Balance at 31 December 2002	✓	✓	✓	✓	✓	B
Charged to income statement	✓	✓	✓	✓	✓	B
Additional provisions - normal	✓	✓	✓	✓	✓	B
Additional provisions - capital gains tax	✓	✓	✓	✓	✓	B
Prior year adjustment by subsidiary	✓	✓	✓	✓	✓	B
Acquisition of subsidiaries	✓	✓	✓	✓	✓	B
Utilised during the year	✓	✓	✓	✓	✓	B
Balance at 31 December 2003	✓	✓	✓	✓	✓	B
None of the items included in the provisions is individually material.	✓	X	X	X	X	B
20. TRADE AND OTHER RECEIVABLES						
Premiums receivable	✓	✓	✓	✓	✓	B
Accrued investment income	✓	✓	✓	✓	✓	B
Trading account and money market investments	✓	✓	✓	✓	✓	B
Accounts receivable	✓	✓	✓	✓	✓	B
Total trade and other receivables	✓	✓	✓	✓	✓	B
21. SHARE CAPITAL AND PREMIUM						
Authorised share capital						
xxx million ordinary shares of x xxx each	✓	✓	✓	✓	✓	B
Issued share capital and premium						
Number of ordinary shares in issue						
Total shares in issue	✓	✓	✓	✓	✓	B
Shares held by subsidiaries	✓	✓	✓	✓	✓	B
Balance at end of year	✓	✓	✓	✓	✓	B
Nominal value and share premium						
Nominal value of xx cent per share	✓	✓	✓	✓	✓	B
Share premium	✓	✓	✓	✓	✓	B
Treasury shares (held by subsidiary)	✓	✓	✓	✓	✓	B
Total nominal value and share premium	✓	✓	✓	✓	✓	B
Authorised and unissued shares						
Subject to the restrictions imposed by the Companies Act, the authorised and unissued shares are under the control of the directors until the forthcoming annual general meeting.	✓	✓	✓	✓	✓	B
Executive share incentive scheme						
Restricted shares and share options at the beginning of the year	✓	✓	✓	✓	✓	B
New options granted	✓	✓	✓	✓	✓	B
Restricted shares cancelled and options granted for the conversion of the Gensec share scheme	✓	✓	✓	✓	✓	B
Unconditional options and shares released, available for release, or taken up	✓	✓	✓	✓	✓	B
Options lapsed or cancelled	✓	✓	✓	✓	✓	B
Cash dividends received on restricted shares and converted into shares	✓	✓	✓	✓	✓	B
Restricted shares and share options at the end of the year	✓	✓	✓	✓	✓	B
Details regarding the restricted shares and share options outstanding on 31 December 2003 and the financial years during which they become unconditional, are as follows:						
Unconditional during year ended						
31 December 2004 (Number of shares, Options, Average option price)	✓	✓	✓	✓	✓	B
31 December 2005 (Number of shares, Options, Average option price)	✓	✓	✓	✓	✓	B
31 December 2006 (Number of shares, Options, Average option price)	✓	✓	✓	✓	✓	B
31 December 2007 (Number of shares, Options, Average option price)	✓	✓	✓	✓	✓	B
31 December 2008 (Number of shares, Options, Average option price)	✓	✓	✓	✓	✓	B
31 December 2009 and later (Number of shares, Options, Average option price)	✓	✓	✓	✓	✓	B

Notes to the Group financial statements

	SLM 2002	OML 2002	LIB 2002	MOM 2002	NAC 2002	Class
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23. LONG TERM INSURANCE POLICY LIABILITIES**23.1 Analysis of movement in policy liabilities**

Income	✓	X	X	X	X	A (4.2)
Premium income (note 23.2)	✓	X	X	X	✓	A (4.3)
Investment surpluses (note 23.3)	✓	X	X	X	X	A (4.2)
Outflow	✓	X	X	X		A (4.2)
Policy benefits (note 23.4)	✓	X	X	X	✓	A (4.3)
Retirement fund terminations	✓	X	X	X	X	A (4.2)
Transfer to segregated assets	✓	X	X	X	X	A (4.2)
Taxation (note 23.5)	✓	X	X	X	X	A (4.2)
Fees, risk premiums and other payments to shareholders' funds	✓	X	X	X	✓	A (4.2)
Net movement for the year	✓	✓	✓	✓	✓	A (4.2)
Balance at beginning of the year	✓	✓	✓	✓	✓	A (4.2)
Balance at end of the year	✓	✓	✓	✓	✓	A (4.2)

Detail of income and expenses relating to Shareholders' funds and Policyholders' funds can be distinguished in Income statement and notes

✓	X	✓	X	✓	A (4.3)
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23.2 Analysis of premium income

Individual insurance						
Recurring	✓	✓	✓	✓	✓	A (4.3)
Single	✓	✓	✓	✓	✓	A (4.3)
Continuations	✓	✓	✓	✓	✓	A (4.3)
Group business						
Recurring	✓	✓	✓	✓	✓	A (4.3)
Single	✓	✓	✓	✓	✓	A (4.3)
Total premium income	✓	✓	✓	✓	✓	A (4.3)

23.3 Investment return: policyholders' funds

Investment income						
Interest-bearing investments	✓	X	✓	X	✓	A (4.2)
Equities	✓	X	✓	X	✓	A (4.2)
Properties	✓	X	✓	X	✓	A (4.2)
Total investment income						
Equity-accounted earnings	✓	N/A	✓	X	N/A	A (4.2)
Net investment surpluses	✓	X	✓	X	✓	A (4.2)
Total investment return	✓	X	✓	X	✓	A (4.2)

23.4 Analysis of long term insurance policy benefits

Individual insurance						
Maturity benefits	✓	X	✓	✓	✓	A (4.3)
Surrenders	✓	X	✓	✓	✓	A (4.3)
Life and term annuities	✓	X	✓	✓	✓	A (4.3)
Death and disability benefits	✓	X	✓	✓	✓	A (4.3)
Cash bonuses	✓	X	✓	✓	✓	A (4.3)
Group business						
Withdrawal benefits	✓	X	✓	✓	✓	A (4.3)
Pensions	✓	X	✓	✓	✓	A (4.3)
Lump-sum retirement benefits	✓	X	✓	✓	✓	A (4.3)
Taxation paid on behalf of certain retirement funds	✓	X	✓	✓	✓	A (4.3)
Death and disability benefits	✓	X	✓	✓	✓	A (4.3)
Cash bonuses	✓	X	✓	✓	✓	A (4.3)
Total long term insurance policy benefits	✓	✓	✓	✓	✓	A (4.3)

23.5 Taxation: policyholders' funds

Normal tax - RSA	✓	X	✓	X	✓	A (4.9)
- Foreign	✓	X	✓	X	✓	A (4.9)
Share of associated company's tax charge	✓	N/A	N/A	X	N/A	A (4.9)
Other						
Taxation on retirement funds	✓	X	✓	X	✓	A (4.9)
Withholding tax on foreign investments	✓	X	✓	X	✓	A (4.9)
Indirect taxation	✓	X	✓	X	N/A	A (4.9)
Total taxation: policyholders' funds	✓	X	✓	X	✓	A (4.9)

A deferred tax asset has not been recognised for estimated assessed losses in the policyholders' tax funds as it is uncertain whether and when these losses will be utilised.

✓	X	X	X	X	A (4.9)
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Notes to the Group financial statements

	SLM 2002	OML 2002	LIB 2002	MOM 2002	NAC 2002	Class
23.6 Composition of policy liabilities						
Individual insurance	✓	X	✓	✓	✓	A (4.6)
Market-related liabilities	✓	X	✓	✓	✓	A (4.6)
Stable bonus fund	✓	X	✓	✓	✓	A (4.6)
Reversionary bonus policies	✓	X	✓	✓	✓	A (4.6)
Non-participating annuities	✓	X	✓	✓	✓	A (4.6)
Other non-market-related liabilities	✓	X	✓	✓	✓	A (4.6)
Group business	✓	X	X	✓	X	A (4.6)
Market-related liabilities	✓	X	X	✓	X	A (4.6)
Stable bonus portfolios	✓	X	X	✓	X	A (4.6)
Participating annuities	✓	X	X	✓	X	A (4.6)
Non-participating annuities	✓	X	X	✓	X	A (4.6)
Other non-market-related liabilities	✓	X	X	✓	X	A (4.6)
Total policy liabilities	✓	X	✓	✓	✓	A (4.6)
23.7 Policy liabilities include the following:						
HIV/Aids reserve	✓	X	✓	✓	✓	A (4.6)
Reduction in earnings caused by using a retrospective HIV/Aids valuation basis instead of a prospective valuation basis	✓	X	X	X	X	A (4.6)
Asset mismatch reserve	✓	X	X	X	X	A (4.6)
Deferred capital gains tax	✓	X	✓	X	✓	A (4.9)
24. OTHER LONG TERM LIABILITIES						
Redeemable cumulative non-voting preference shares issued by subsidiary companies with dividend terms which are linked to prime interest rates and with different redemption dates up to xxxx	✓	X	X	✓	X	B
Obligation for post-retirement medical fund contributions in respect of clients – matched by assets held in this regard	✓	X	X	✓	X	B
Secured bank loans at interest rates of between xx% and xx% (2001: xx% and xx%) and repayable in equal xxxx and xxxx instalments over xx to xx (2001: xx to xx) years. Secured by term loans and deposits included in Investments	✓	X	X	✓	X	B
Unsecured debt securities with interest rates varying between x% and x%	✓	X	X	✓	X	B
Secured loan notes in the amount of xx million and xx million, bearing interest at variable interest rates. At year-end these rates were x% and x% (2001: x%). The loan notes are ultimately repayable on xxxx and xxxx respectively.	✓	X	X	✓	X	B
Other	✓	X	X	✓	X	B
Total other long term liabilities	✓	X	X	✓	X	B
Portion potentially repayable within one year included above	✓	X	X	✓	X	B
25. TRADE AND OTHER PAYABLES						
Trading account and money market liabilities	✓	✓	All disclosed on face of Balance sheet	All disclosed on face of Balance sheet	✓	B
Accounts payable	✓	✓			✓	B
Policy benefits payable	✓	✓			✓	B
Claims incurred but not reported	✓	✓			✓	A (Note 1)
Total trade and other payables	✓	✓	✓	✓	✓	B
EXTRA: PRESENT VALUE OF ACQUIRED IN-FORCE BUSINESS						
Cost	Information disclosed in Embedded Value Report	✓	Information disclosed in Embedded Value Report	Information disclosed in Embedded Value Report	Information disclosed in Embedded Value Report	
Amortisation for the year		✓				A (4.6)
Net book value		✓				
EXTRA: DEFERRED ACQUISITION COSTS						
Cost	Information disclosed in Embedded Value Report	✓	Information disclosed in Embedded Value Report	Information disclosed in Embedded Value Report	Information disclosed in Embedded Value Report	
Amortisation for the year		✓				A (4.6)
Net book value		✓				
New business premium income (included in note 23.2)	✓	✓	✓	X	X	A (4.8)

Note 1: Claims incurred but not reported are disclosed by all the insurers selected in the comparability test and no non-comparability was found. This was not seen as a separate material industry-specific element and the valuation and earnings reporting as discussed under part of 4.3 and 4.5 includes this.

Notes to the Group financial statements	SLM 2002	OML 2002	LIB 2002	MOM 2002	NAC 2002	Class
26. PAYMENTS TO CLIENTS						
Total payments to clients (Policyholders' funds and Shareholders' funds)	✓	✓	✓	✓	✓	A (4.7)
27. FINANCIAL INSTRUMENTS						
Derivative financial instruments						
In connection with its current operating activities, the Group is exposed to various financial risks, such as foreign currency risk, interest rate risk, credit risk, market risk and liquidity risk. For the management of financial risks, the Group uses derivative financial instruments.	✓	✓	✓	✓	✓	B
Quantified in Rands:						
Residual term to contractual maturity					Polyholders'- and Shareholders' funds shown separately	
Total notional amounts	✓	✓	✓		✓	B
Asset liability management						
Total fair value of amounts						
Interest rate products over the counter	✓	✓	✓	✓	✓	B
Total interest rate products	✓	✓	✓	✓	✓	B
Market risk products	✓	✓	✓	✓	✓	B
Total market risk products	✓	✓	✓	✓	✓	B
Foreign exchange products over the counter	✓	✓	✓	✓	✓	B
Total foreign exchange products	✓	✓	✓	✓	✓	B
Securities lending	✓	X	X	✓	X	A (4.5)
Market risk - interest and equities	✓	X	✓	✓	✓	B
Currency risk	✓	X	✓	✓	✓	B
Credit risk	✓	X	✓	✓	✓	B
Liquidity risk	✓	X	✓	✓	X	B
Underwriting risk	✓	X	✓	✓	✓	A (4.5)
Legal risk	✓	X	✓	X	X	A (4.5)
Cash flow risk	X	X	✓	X	X	B
Investment risk	X	X	✓	X	X	B
Claims risk	X	X	✓	X	X	A (4.5)
Operational risk	X	X	✓	✓	X	A (4.5)
Tax risk	X	X	✓	X	X	A (4.5)
Property risk and hedging risk	X	X	X	X	✓	A (4.5)
Capital adequacy risk	✓	X	✓	X	✓	A (4.5)
28. TANGIBLE NET ASSET VALUE PER SHARE						
Tangible net asset value per share is calculated on the Group shareholders' funds of R xxx million (2001: Rxxx million), after adjusting for the shareholders' interest in subsidiaries from net asset value to fair value, divided by xxx million (2001: xxx million) shares (refer note 21)	✓	X	X	✓	X	B
29. RETIREMENT BENEFITS FOR EMPLOYEES						
Retirement provision	✓	✓	✓	✓	✓	B
Defined contribution funds	✓	✓	✓	✓	✓	B
Defined benefit funds	✓	✓	✓	✓	✓	B
Medical aid funds	✓	✓	✓	✓	✓	B
Principal actuarial assumptions disclosed	✓	✓	✓	✓	X	B
Based on reasonable actuarial assumptions about future experience, the employers' contribution as a fairly constant percentage of the remuneration of the members of the funds should be sufficient to meet the promised benefits of the funds.	✓	✓	✓	✓	✓	B
Funded status						
The funded status of the funds were as follows:						
Actuarial value of fund assets	✓	✓	✓	✓	✓	B
Present value of accrued retirement benefits	✓	✓	✓	✓	X	B
Present value of unfunded obligation	✓	✓	✓	✓	X	B
Net assets	✓	✓	✓	✓	✓	B
Unrecognised surplus	✓	✓	✓	✓	X	B
Net liability included on balance sheet	✓	✓	✓	✓	X	B
Movements in the net liability recognised in the balance sheet are as follows:						
Net liability at start of year	✓	✓	✓	✓	X	B
Net expenses recognised in the income statement	✓	✓	✓	✓	X	B
Contributions	✓	✓	✓	✓	X	B
Net liability at end of year	✓	✓	✓	✓	X	B
The actual return on the market value of the assets as at 31 December 2002 was						
The above value of fund assets includes an investment of Rxx million in Holding company shares.						
The actuarial surplus is currently not recognised as an asset by the Group, as the extent of the surplus available to the company cannot be determined with certainty.	✓	✓	✓	✓	X	B
The valuation of the defined benefit funds for 2001 was performed on x xxxxx xxx.						

Notes to the Group financial statements	SLM 2002	OML 2002	LIB 2002	MOM 2002	NAC 2002	Class
30. BORROWING POWERS						
In terms of the articles of association of the Holding company, the directors may at their discretion raise or borrow money for the purpose of the business of the company without limitation.	✓	x	✓	x	x	B
31. COMMITMENTS AND CONTINGENCIES						
Details and period due of commitments and contingencies	✓	✓	✓	✓	✓	B
Total operating lease commitments	✓	✓	✓	✓	x	B
32. RELATED PARTY TRANSACTIONS						
Details of related party transactions	✓	✓	✓	✓	✓	B
33. NOTES TO THE CASH FLOW STATEMENT						
33.1 Cash generated from operations	✓	✓	✓	✓	✓	B
33.2 Acquisition of subsidiaries	✓	✓	✓	x	✓	B
33.3 Cash utilised in policyholder activities	✓	✓	x	x	x	B
33.4 Cash from financing	✓	✓	✓	x	x	B
EXTRA: POST BALANCE SHEET EVENTS (In Directors' report)	✓	✓	✓	✓	✓	B
EXTRA: SCRIP LENDING ARRANGEMENTS						
Details, Market value, Value of collateral (details of collateral - cash, bonds and Money Market, equities), collateral %	x	x	x	✓	✓	B

