

Financial Reporting Practices in the Insurance Company in Bangladesh: An Evaluation of the Implementation of IFRS 4, Insurance Contract

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Abstract

The wave of globalization has touched in every edge of the world and also proceeds in business world. Business uses accounting standard for preparing financial statements to examine the purpose of it. Financial globalization proceeds, International Financial Standard are increasingly becoming important instruments of integration. Meanwhile, International Financial Reporting Standards (IFRS) provides evidence of accounting quality for economic consequences. IFRS argues the purpose of financial reporting is essential to reduce information asymmetry between corporate manager of companies and parties contracting with firm. This has been observed in development countries whose are leading engine in the world. Different renowned economic forum and organization reinforced the influence of implementation of IFRS in which they called global accounting standards by 2011. By the end of 2008, there were over 100 countries that had adopted IFRS. Among IFRSs, IFRS 4 requires insurance contract to comply with international accounting standards for financial reporting in order to give improvements to accounting practice and to understand the salient aspects that are related to insurance company.

Keywords: Insurance contract; IFRS; IAS; Accounting Standard; Disclosure Checklist

Introduction

Worldwide growth of public concern for insurance business, it has been one of the most important developments in recent decades. Insurance has helped to connect with societies and individual more closely than ever before. Insurance service is different from other services, as it is complex and future contingent service involves substantial legal characteristics. Insurance business is not new in Bangladesh, almost a century back, during the British rule in India, some insurance companies started insurance business transaction, both life and general insurance, in this region (former Bangla or Indian Subcontinent). At the same time, absence of adoption IFRS increasingly transcends national borders and pose serious challenges to the health of the insurance business. The development of more effective insurance laws and regulation in Bangladesh, throughout the world has thus become critical to directing economic development and growth onto a path of insurance business sustainability. Different insurance companies of Bangladesh provide different types of insurance policy which helps to develop the industry, individual, attract foreign investment, contribution to GDP. It's also to develop the standard of living. Like other organizations, it fulfills their duties & put their contribution in national income and make the financial market healthy. Though, insurance industry has significant prospects in the economy but for some reasons, it has failed to achieve its goal to some extent. Besides, the huge prospects of the insurance companies while should fully practices of IFRSs for preparing financial statements. This study makes a critical appraisal of the contemporary insurance business and examine whether IFRS 4 can contribute towards the monitoring and the progress as well as making world wide the insurance business. This work concentrates on the importance of practices and application of IFRS 4 for insurance business in relating thereto for developing country- Bangladesh.

Prospects of the study

Risk which is uncertainty regarding loss, pose a problem to business and individual in nearly every walk of life. Risk is something that is now taken up upfront rather than be left to fare to decide. Insurance is a

system of spreading the risk of one on the shoulders of many. Ahmed and Khanal [1] argued that the scope of insurance business is diversified and many sectors are fully or partially dependent on insurance e.g., import-export, agriculture, real estate, garments industry, service sector as well as overall business of the country are completely dependent on its sound operation. Thus, it is clear that insurance company minimize the risk and uncertainty but insurance may fallen down in risk if they do not practices and applies themselves mostly accepted accounting standard that is becoming the global standard. Specially, IFRSs are a set of accounting standard developed by the International Accounting Standards Board (IASB) by the preparation of public company's financial statement [2].

Financial standards are prepared and presented for external users by the entries around the world. It has been extended to insurance business' financial reporting for the business entities. Although, such financial statements may appear similar from country to country, if there are various difference due to variety of social economy and legal circumstances and by different countries having in mind the needs of different users of financial statements when setting national requirements.

Over the years the business community has admitted that the accounting of "the language of business" and financial information is a form of language. And undoubtedly to ensure its usefulness, financial information should not only be intelligible, but also be comparable so that investment and credit decision can more readily be taken. Over the past few decades, the accounting profession has been facing the pressure

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of globalization and continuously seeking the way to community. A set of International Accounting Standard of business in Bangladesh will allow new horizons of evolution due to the that comparative analysis of the areas of returns established based on the balance sheet and profit and loss account between the companies being in competition become relevant. One of the perceived benefits of a single set of high quality, globally accepted accounting standards is that investors can read a set of financial statements of companies and understand the financial result. Since, IFRS is being incorporated into an increasing number of countries that will have perspectives about the application of IFRS.

By adopting IFRS, all insurance companies in Bangladesh can present its financial statements on the same basis as its foreign competitors, making comparisons easier. Accounting theory argues that the purpose of financial reporting is essential to reduce information asymmetry between corporate manager and parties constricting with their firm. Furthermore, insurance companies with subsidiaries in countries that require or permit IFRS may be able to use one accounting language country wide.

Literature Review

There are some literatures which explored with IFRS disclosures requirement. In Bangladesh, the accounting disclosure has yet to be studied vigorously [3]. However, does not mean that this issue is unimportant, and lately a lot of researchers have been researching on the report of extraordinary item [4], cash flow statement [5], empirical studies on accounting and disclosure [6], uses of financial report [7], and information that are needed by consumer and voluntarily disclosure by Dhaka Stock Exchange (DSE) listed companies [8]. Ahmed [9], investigated that disclosure of information for the banking sector in Bangladesh has not been increased over the last two decades. The regulatory frameworks set minimum legal requirements as to the disclosure of accounting information in corporate annual reports and are likely, therefore to produce statements which are confined only to concepts of 'minimum disclosure'. Wise and Ali [10] depicted that if corporate social responsibility disclosure is made obligatory there is a strong case for it to follow international benchmarks. Alsafadi and Abualola [11] examined the application of IFRS 4 (Insurance Contracts) in Gaza insurance organizations. This standard requires entities that issues insurance contracts to make limited improvements to accounting by insurers for insurance contracts, and to the disclosure that identifies and explains the amounts in an insurer's financial statements arising from insurance contracts. Nurunnabi [12], made this research is to explore the implementation of IFRSs in a developing country, emphasizing the impact of accounting regulatory frameworks, politico-institutional factors, cultural factors, training opportunities in the accounting profession and corruption.

IFRS 4, Insurance Contract

The IFRS 4 Insurance Contracts is especially for clarification of accounting treatments for insurance contracts. This IFRS describes the detailed accounting and financial reporting treatment relating insurance contract in the financial statements [13].

The objective of this IFRS is to specify the financial reporting for insurance contracts by any entity that issues such contracts (described in this IFRS as an insurer) until the Board completes the second phase of its project on insurance contracts. In particular, IFRS 4 requires:

a) Limited improvements to accounting by insurers for insurance contracts.

b) Disclosure that identifies and explains the amounts in an insurer's financial statements arising from insurance contracts and helps users of those financial statements understand the amount, timing and uncertainty of future cash flows from insurance contracts.

An insurance contract is 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 future event (the insured event) adversely affects the policyholder.

The IFRS 4 applies to all insurance contracts (including reinsurance contracts) that an entity issues and to reinsurance contracts that it holds, except for specified contracts covered by other IFRSs. It does not apply to other assets and liabilities of an insurer, such as financial assets and financial liabilities within the scope of IAS 39 Financial Instruments: Recognition and Measurement. Furthermore, it does not address accounting by policyholders.

The IFRS 4 exempts an insurer temporarily from some requirements of other IFRSs, including the requirement to consider the Framework in selecting accounting policies for insurance contracts. However, the IFRS 4:

a) Prohibits provisions for possible claims under contracts that are not in existence at the reporting date (such as catastrophe and equalization provisions).

b) Requires a test for the adequacy of recognized insurance liabilities and an impairment test for reinsurance assets.

c) Requires an insurer to keep insurance liabilities in its balance sheet until they are discharged or cancelled, or expire, and to present insurance liabilities without offsetting them against related reinsurance assets.

The IFRS 4 permits an insurer to change its accounting policies for insurance contracts only, as a result, its financial statements present information that is more relevant and no less reliable, or more reliable and no less relevant. In particular, an insurer cannot introduce any of the following practices, although it may continue using accounting policies that involve them:

a) Measuring insurance liabilities on an undiscounted basis.

b) Measuring contractual rights to future investment management fees at an amount that exceeds their fair value as implied by a comparison with current fees charged by other market participants for similar services.

c) Using non-uniform accounting policies for the insurance liabilities of subsidiaries.

The IFRS permits the introduction of an accounting policy that involves remeasuring designated insurance liabilities consistently in each period to reflect current market interest rates (and, if the insurer so elects, other current estimates and assumptions). Without this permission, an insurer would have been required to apply the change in accounting policies consistently to all similar liabilities (Table 1).

The IFRS 4 requires disclosure to help users understand:

(a) The amounts in the insurer's financial statements that arise from insurance contracts.

(b) The amount, timing and uncertainty of future cash flows from insurance contracts.

Sl. No.	Disclosure requirements under IFRS 4	para.
1	Amount shown in financial statement arising from insurance contract	36
2	Accounting policy of insurance contract	37(a)
3	Accounting policy of insurance contract related assets, liability income and expense	37(b)
4	Recognition of assets, liability, income, and expense arising from insurance contract	37(c)
5	Gain and losses recognized in profit or loss on buying reinsurance	37(d)
6	Amortize gain and loss, arising on buying reinsurance	37(e)
7	Amortization, period and amount on buying reinsurance at the end of the period	37(f)
8	Determined assumption that have been used to measure assets and liability arising in insurance contract & reinsurance	37(g)
9	Effect of changes assumption used to measure insurance assets and liability	37(h)
10	Reconciliation of change in insurance liability, assets, if any	37(i)
11	Amount, timing, and uncertainty of future cash flow from insurance contract	38
12	Objective of managing risk arising from insurance contract	39(a)
13	Condition of insurance contract that have material effect of timing, amount and uncertainty	39(b)
14	Information about insurance risk	39(c)
15	Information about interest rate risk, credit risk (IAS 32) required	39(d)
16	Information about expose to interest rate or market risk contained in insurance contract	39(e)
17	No need any disclosure information except IFRS para. 37	42
18	Any impracticable information is exist which will be disclosed	43
19	Any application is firstly application of IFRS that it is practicable will be disclosed	44

Table 1: List of summary of IFRS 4.

Objective of the study

Purpose tells the reason of the task. It always kept focused to be on right track. The main objective of the study is to focus on the practices and implementation of International Accounting Standard by the insurance companies in Bangladesh whereas;

- To appraise the impact of the practicing IFRS 4
- To identify associated problem in the observation and reach to recommend action required to mitigate the problematic situation in the insurance business.
- To focus the role for quality accounting information.
- To identify the major problem faced by the insurance industry due to lack of application of IFRS 4.

Methodology

The study has been conducted mainly on the basis of literature survey and secondary information to identify on usage behavior of insurance company in Bangladesh. Various journals and research paper, diagnostic study report, information from annual report, website and newspaper articles have been studied in making. Consequently, this is grounded data from related companies in the country and regulatory authority. Scoring the items of disclosure index gives tick mark (✓) if it is disclosed and gives cross mark (x) if it is not disclosed. Bhuiyan and Kamal [14-19] argues that the focus of determining whether to use this system is preferable (Table 2).

Analysis and Findings

IAS (International Accounting Standard) -1, Presentation of Financial Statements paragraph 7 prescribes a complete set of financial Statement includes balance sheet, income statement, statement showing either all changes in equity or changes in equity other than those arising from capital transaction with owners and distribution to owners, cash flow statements, and accounting policies and explanatory notes. It was found that the surveyed insurance companies have prepared their Financial Statement as per above standard. IFRS 4,

Sl. No	Name of Companies	Category	Short Form
1	United Insurance Company Ltd.	Gen. Insu	UICL
2	Peoples Insurance Company Ltd.	Gen. Insu	PICL
3	Standard Insurance Ltd	Gen. Insu	SIL
4	Global Insurance Ltd.	Gen. Insu	GIL
5	Northern Gen. Insurance Company Ltd.	Gen. Insu	NGIL
6	Continental Insurance Ltd.	Gen. Insu	CIL
7	Mercantile Insurance Company Ltd.	Gen. Insu	MICL
8	Dhaka Insurance Company Ltd	Gen. Insu	DICL
9	Asia Pacific General insurance Ltd.	Gen. Insu	APGIL
10	Asia Insurance Ltd.	Gen. Insu	AIL

Table 2: List of sample insurance companies.

Insurance Contract contains those mandatory disclosure information items under 19 paragraphs;

Amount shown in financial statement arising from insurance contract, IFRS 4, para. 36

This is the disclose information under IFRS 4 that identifies and explains the amounts in the financial statements arising from insurance contracts. It can be seen (Appendix) that presents the frequency of item disclosed is 100% in the annual reports over the period.

Accounting policy of insurance contract, IFRS 4 para. 37(a)

This accounting policy adopted for insurance contracts and related assets, liabilities, income and expenses. It can be seen from appendix table that the frequency of item disclosure is 90% of selected insurance companies but only the company- Northern General Insurance Company did not disclosed this items.

Accounting policy of insurance contract related assets, liability income and expense, IFRS 4 para. 37 (b)

This policy recognized assets, liabilities, income and expense (and, if the statement of cash flows is presented under the direct method, cash flows) arising from insurance contracts. Furthermore, if the insurer is a cedant, disclose: gains and losses recognized in profit or loss on buying reinsurance; and if the cedant defers and amortizes gains and losses

arising on buying reinsurance, the amortization for the period and the amounts remaining unamortized at the beginning and end of the period. It can be seen (Appendix) and presents the frequency of item disclosure is 100% in the annual reports over the study period.

Recognition of assets, liability, income, and expense arising from insurance contract IFRS 4, para. 37(c)

The policy use to determine the assumptions that have the greatest effect on the measurement of the recognized amounts described in IFRS 4. 37(b); when practicable, give quantified disclosure of those assumptions. It can be seen from appendix table that the frequency of disclosed is 60% of selected companies but United Insurance Company, People Insurance Company, Standard Insurance Company and Mercantile Insurance Company did not disclosed under this items.

Gain and losses recognized in profit or loss on buying reinsurance, IFRS 4 para. 37(d)

The effect of changes in assumptions used to measure insurance assets and insurance liabilities, showing separately the effect of each change that has a material effect on the financial statements. It can be seen from the appendix table, the frequency of item disclosure is 100% in the annual reports.

Amortize gain and loss, arising on buying reinsurance, IFRS 4, para. 37(e)

In this policy reconciliations of changes in insurance liabilities, reinsurance assets and, if any, related deferred acquisition costs. It can be seen (Appendix) the frequency of item disclosure is 30% of selected companies disclosed under this paragraph, but United Insurance Company, Standard Insurance Limited, Northern General Insurance Company, Continental Insurance Limited, Dhaka Insurance Limited, Asia Pacific General Insurance and Asia Insurance Limited did not disclosed this item.

Amortization, period and amount on buying reinsurance at the end of the period, IFRS 4, para. 37(f)

Amortization has been charged on intangible assets for using in the business. Appendix table presents the frequency of items disclosure is 40% in the annual reports, but People Insurance Company, Standard Insurance Limited, Northern General Insurance Company, Continental Insurance Limited, Dhaka Insurance Limited, Asia Insurance Limited did not disclosed this item.

Determined assumption that have been used to measure assets and liability arising in insurance contract and reinsurance, IFRS 4, para. 37(g)

Appendix table presents the frequency of disclosure items is 40% of selected companies under this paragraph, but Standard Insurance Limited, Global Insurance Limited, Northern General Insurance Company, Continental Insurance Limited, Dhaka Insurance Limited, and Asia Pacific General Insurance did not disclosed this items.

Effect of changes assumption used to measure insurance assets and liability, IFRS 4, para. 37 (h)

This policy indentifies the effect of changes assumption used to measure insurance assets and liability. The findings of the checklist that no disclosure items have been disclosed among the companies.

Reconciliation of change in insurance liability, assets, if any, IFRS 4, para. 37(i)

Under this paragraph covered the reconciliation of change in insurance liability, assets. The finding of checklist that no item has been disclosed of selected companies.

Amount, timing, and uncertainty of future cash flow from insurance contract, IFRS 4, para. 38

Under this paragraph developed amount, timing, and uncertainty of future cash flow from insurance contract. It can be seen from the checklist the frequency of item disclosure is only 10% of selected companies which is Standard Insurance Limited disclosed this item.

Objective of managing risk arising from insurance contract, IFRS 4, para. 39 (a)

The findings from appendix table presents the frequency of item disclosure items are 70% in the annual reports but, United Insurance Company, Continental Insurance Limited, and Mercantile Insurance Company did not disclosed this item.

Condition of insurance contract that have material effect of timing, amount and uncertainty, IFRS 4, para. 39(b)

This policy argued the condition of insurance contract that have material effect of timing, amount and uncertainty. The findings of the checklist shown that no item has been disclosed.

Information about insurance risk, IFRS 4, para. 39 (c)

As indicated in the appendix table, that the 40% of selected companies have disclosed this items in the annual report, but People Insurance Company, Standard Insurance Limited, Global Insurance Limited, Northern General Insurance Company, Dhaka Insurance Limited and Asia Pacific General Insurance did not disclosed this item.

Information about interest rate risk, credit risk (IAS 32) required, IFRS 4, para. 39(d)

It can be seen from the paragraph that information about interest rate risk, credit risk (IAS 32). Appendix table presents the frequency of item disclosure is 10% of selected companies, only United Insurance Company disclosed this item.

Information about expose to interest rate or market risk contained in insurance contract, IFRS 4, para. 39(e)

Under this paragraph, it can be seen from the appendix table the frequency of item disclosure is 20% of selected companies, only United Insurance Company, and Mercantile Insurance Company disclosed this item.

No need any disclosure information except, IFRS 4, para. 42

The findings of checklist shown that no companies disclosed this item.

Any impracticable information is exist which will be disclosed, IFRS 4, para. 43

The findings of checklist shown that no companies disclosed this item.

Any application is firstly application of IFRS that it is practicable will be disclosed, IFRS 4, para. 44

This policy presents for actual claims disclosed in accordance with

Disclosure	UIC	PIC	SIL	GIL	NGIC	CIL	MIC	DIL	APGI	AIL	Pool
requirements under IFRS 4											
Disclosure requirements	19	19	19	19	19	19	19	19	19	19	190
Disclosure items	8	7	6	8	5	6	8	6	8	8	70
Disclosure percentages	42.1	36.84	31.6	42.1	26.32	32	42.1	31.6	42.1	42.1	36.84

Table 3: Aggregate level of Disclosure Index.

IFRS 4. 39(c) (iii), information about claims development that occurred earlier than five years before the end of the first financial year need not be disclosed. The findings of checklist shown that no companies disclosed this item (Table 3).

Table 3 presents that the total disclosure items under IFRS 4 of selected insurance companies, where are total 19 paragraphs. It has seen that the highest score 42.1% which are disclosed five insurance companies; United Insurance Company, Global Insurance Limited, Mercantile Insurance Company, Asia Pacific General Insurance, and Asia Insurance Limited. And the lowest score is 31.6% which are disclosed two companies; Standard Insurance Limited and Dhaka Insurance Limited. The average level of disclosure score is 36.84% for selected 10 sample companies.

Recommendation

In a developing country, Bangladesh prospect can figure out the following recommendations that may accrued by the practicing of IFRS 4. This recommendation might facilitates the enactment of a new Financial Reporting environment and the repeal of the provisions on accounting and financial reporting considering Companies Act 1994, Insurance Companies Act 2010 and other related regulations;

a) The practices may have some direct impact on the corporate sector especially insurance company. Agency problem between management and shareholders can be substantially reduced through implementation of IFRS as increased transparency causes manager to act more in the interest of the shareholder. The increased transparency promised by IFRS also could cause a similar increase in the efficiency of contracting between firms and lenders.

b) IFRS practices could reduce the cost of investors of processing financial information. Improving financial reporting quality allows the small investors to complete better with professional and hence reduce the risk they are trading with a better-informed professional.

c) By adopting IFRS, a business can present its financial statements on the same basis as its foreign competitors, making comparisons easier. Companies also may need to convert to IFRS if they are a subsidiary of a foreign company that must use IFRS, or if they have a foreign investor that must use IFRS. Companies may also benefit by using IFRS if they wish to raise capital abroad.

Besides, those of practicing IFRS, insurance company in Bangladesh may have another suggestion are awaiting as;

a) The conduct transparent and high quality information for General as well as Life insurance service.

b) To create best values for customers, shareholders and all stakeholders.

c) To utilize stronger International Standards driven initiative in order to meet their challenges and requirements of the company and its clients.

d) To improve administrative and organizational configuration

in order to prepare the platform for the best practices of corporate governance.

e) To meet the various insurance needs of the community that would arise in changing socials and economic environment.

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