



Institute
and Faculty
of Actuaries

2nd Exposure Draft of ISAP 4 on IFRS 17 Insurance Contracts

IFoA response to the International Actuarial
Association

30 April 2019

About the Institute and Faculty of Actuaries

The Institute and Faculty of Actuaries (IFoA) is a royal chartered, not-for-profit, professional body. We represent and regulate over 32,000 actuaries worldwide, and oversee their education at all stages of qualification and development throughout their careers.

We strive to act in the public interest by speaking out on issues where actuaries have the expertise to provide analysis and insight on public policy issues. To fulfil the requirements of our Charter, the IFoA maintains a Public Affairs function, which represents the views of the profession to Government, policymakers, regulators and other stakeholders, in order to shape public policy.

Actuarial science is founded on mathematical and statistical techniques used in insurance, pension fund management and investment. Actuaries provide commercial, financial and prudential advice on the management of assets and liabilities, particularly over the long term, and this long term view is reflected in our approach to analysing policy developments. A rigorous examination system, programme of continuous professional development and a professional code of conduct supports high standards and reflects the significant role of the profession in society.



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Please use this template to comment on the [2nd Exposure Draft of ISAP 4 on IFRS 17 Insurance Contracts](#), and the proposed revisions to the [Glossary for ISAP 4](#).

The IAA invites comments on this 2nd Exposure Draft, particularly on the questions set out below. Comments are most helpful if they:

- (a) Are comments on the questions as stated;
- (b) Take full account of what is already addressed in the [consultation report on the 1st exposure draft](#).
- (b) Indicate the specific paragraph or group of paragraphs to which they relate;
- (c) Contain a clear rationale; and
- (d) Include any alternative that the IAA should consider, if applicable within the scope of the [Statement of Intent for ISAP 4](#).

Identification and instructions		
Name of Individual:	Please indicate if your comments are personal, or represent your organization:	Represent organisation.
Name of organization		Institute & Faculty of Actuaries (IFoA).
Disclosure of comments:	Please indicate if your comments should be treated as confidential, and if so why:	N/A
Instructions for filling in and sending the template	<p>Please follow the following instructions for filling in the template:</p> <ul style="list-style-type: none"> ⇒ Do not write in the yellow shaded cells ⇒ Write in the white cells ⇒ When commenting on a specific paragraph: <ul style="list-style-type: none"> ○ Please use a separate row for each paragraph, sub paragraph, or bullet. ○ Please include the full reference in the first column such as “Introduction 3rd paragraph 2nd bullet” or “2.6.1.b.ii” ○ Please insert/append extra rows as needed. <p>Please send the completed template, renamed with the organization’s or individual’s name, attached in <u>Word Format</u>, to ISAP4.comments@actuaries.org</p>	



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	Specific Questions asked by the ASC	Response
Q1.	Is the guidance clear and unambiguous? If not, how should it be changed?	Overall, our view is that the ISAP is clear. However, we have noted some specific areas where clarity could be improved.
Q2.	Is the guidance sufficient and appropriate? If not, how should it be changed?	<p>It may be helpful to improve the balance of the content between IFRS 17 topics, as noted in our general comments below.</p> <p>We would suggest reviewing the ISAP following the Transitional Resource Group (TRG) discussions and the changes being proposed by the IASB in the forthcoming exposure draft of the standard. Examples of this have been provided in the comments below.</p>

	General Comments on the ISAP 4 – 2 nd Exposure Draft
	<p>We appreciate the effort that has gone into reviewing the comments provided on the first exposure draft of ISAP 4, and welcome the changes made in response. In particular, we have considered the report on the treatment of comments on the first exposure draft, and have take into account the detailed responses provided here.</p> <p>We recognise the effort involved in revising the wording. In our view these revisions significantly improve the clarity and relevance of the ISAP for actuaries providing services related to IFRS 17.</p> <p>We have made some specific comments below. We suggest that the balance of the content included in ISAP 4 covering specific aspects of IFRS 17 could be reconsidered to reflect the areas of activities that actuaries are likely to be involved in. For example:</p> <ul style="list-style-type: none"> • there is significant content on the measurement of reinsurance contracts (paragraphs 2.6.6 and 2.6.7) relative to other aspects;



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	<ul style="list-style-type: none"> less content is given on the subsequent measurement of contracts using the Variable Fee Approach, compared to other measurement approaches; and the ISAP sets out the impracticability of the full retrospective approach, but guidance on modified retrospective approaches and the fair value approach is not provided. <p>Additionally, it may also be helpful for the ISAP to include the allocation of modelled actuarial results and accounting information to the appropriate level of granularity for measurement of insurance contract groups. This would be relevant to both the:</p> <ul style="list-style-type: none"> current measurement of insurance contract balances (i.e. inclusion as additional requirement in paragraph 2.6.14); and determination of transition balances (i.e. inclusion as additional requirement in paragraph 2.10).
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Comments on specific paragraphs of the ISAP 4 - 2 nd Exposure Draft		
Full paragraph reference	Change proposed to the paragraph (markup preferred)	Reason the change is needed (can be kept very brief or left blank if obvious from the change)
1.2	<p>Proposed alternative text with edits in red:</p> <p><i>Scope – This ISAP applies to actuaries when performing actuarial services related to IFRS 17 for the preparation of an entity’s actual or pro-forma IFRS financial statements, and to actuaries performing other actuarial services in connection with IFRS 17 (for example: an actuary advising a third party such as an auditor or a regulator, or advising a potential buyer regarding an acquisition). Actuaries should apply the guidance in this ISAP to the extent relevant to the assignment.</i></p>	<p>We would suggest that adding the proposed edits may refine the scope of the ISAP.</p> <p>The current wording could imply that actuaries are required to comply with every requirement in the ISAP, even when the scope of activities related to the preparation of IFRS financial statements is limited to a specific area of the standard.</p> <p>For example, actuaries are not required to detail changes in classification and aggregation (per paragraph 2.4) in a written report, where their work is</p>



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		limited to the setting of assumptions related to estimating fulfilment cash flows that has no effect on classification and aggregation.
2.6.1a	Proposed alternative text with edits in red: <i>Combining coverages with similar risks based on the nature of the insurance obligation, without the assumption setting process being unnecessarily constrained by the grouping of insurance contracts chosen for IFRS 17 measurement purposes</i>	We have suggested some additional wording that could help to improve clarity: the grouping could follow logically from the contract risk profile.
2.6.1e	Proposed deleted text in red: The use of credibility techniques when combining information from various sources or time periods;	We suggest that as it is not necessary to require consideration of credibility techniques, this point could be omitted. This is one of many techniques that could be reliably used to determine assumptions using multiple sources of data. An alternative could be wording that appears in ISAP 1 (2.7.1): 'The actuary could consider to what extent it is appropriate to adjust assumptions or methodology to compensate for known deficiencies in the available data'.
2.6.2	We refer to the text: <i>Process for Updating Assumptions – If the actuary considers it appropriate to change the process, including the methodology, used to update a recommended assumption, the actuary should discuss the change with the principal, including whether it would constitute a change in accounting policy or just a change in an accounting estimate as defined in IAS</i>	In our view this could be interpreted as implying that for any change in any part of the process of setting any assumptions, the actuary has to discuss this with the principal and check against IAS 8, giving both the rationale and the impact. We note that materiality and proportionality are



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	<i>8 Accounting Policies, Changes in Accounting Estimates and Errors.</i>	considered implicit in every paragraph. However, it may still be helpful to mention considerations around materiality and proportionality here.
2.6.3	We refer to the text: <i>Insurance Risks – When advising the principal or the entity on assumptions to measure insurance risks, the actuary should consider relevant factors including the following ...</i>	We note that the measurement of insurance risks could refer to many aspects of IFRS 17 measurement; for example, the measurement of the estimate of future cash flows and/ or the measurement of the risk adjustment. It may therefore be useful to clarify or expand this section.
2.6.9	We refer to the text: <i>Discount Rates – The actuary should when advising the principal or the entity on the derivation of:</i> <i>Discount rates for:</i> <i>(i) Periods beyond those for which observable data from a deep and liquid market is available, consider how current rates are expected to evolve over time using the best information available in the circumstances, including such market prices as are observable; and ...</i>	We note that the text on discount rates refers to extrapolation. It may also be helpful to include wording on interpolation and requirements to derive weighted average locked-in discount rates (for the general model), which will also require actuarial involvement.
2.6.10	We refer to the text: <i>Contracts with Cash Flows that Vary with Returns on Underlying Items - When advising the principal or the entity, the actuary should:</i> <i>Select discount rates used to calculate the present value of the cash flows to measure the fulfilment cash flows that reflect the returns anticipated in the estimates of the future cash flows. Returns on assets should be estimated using prospective expectations consistent with current market expectations of future economic conditions ...</i>	In our view this could imply that cash flows varying with underlying items need to be measured separately using different projection and discounting assumptions. However, IFRS 17.B77 notes that entities are not required to divide cash flows between those that vary with underlying items and those that do not vary with underlying items when determining discount rate assumptions. The guidance could be updated to reflect



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		this.
2.6.13b i	<p>We refer to the text:</p> <p><i>In assessing what the entity requires as compensation for bearing the non-financial risks:</i></p> <p>i. <i>Reflect the diversification benefit at the relevant level of consolidation</i></p>	<p>It may be helpful to reflect the discussion in the May 2018 IASB TRG AP02; this describes the use of a single view of diversification that does not change when considering an entity, versus consolidated group financial statements.</p> <p>We would propose that:</p> <p>(b)(i) suggests a different degree of diversification at group and entity levels; and</p> <p>c (iii) could be reworded to ‘<i>allows for diversification commensurate with how the entity factors diversification benefits into its decision making processes</i>’.</p> <p>We note that, aside of the determination of the risk adjustment, there are other reasons why IFRS 17 contract measurement would differ when determined for a single reporting entity versus consolidated group financial statements (e.g. impact of different entity and group reporting frequencies, internal reinsurance, internal service company arrangements et al).</p> <p>This difference in treatment could potentially be highlighted in the ISAP.</p>
2.6.13e	<p>We refer to the text:</p> <p><i>Allow for the uncertainty caused by the potential of non-performance by reinsurers either in the estimates of future cash flows to be received from reinsurance contracts or in the</i></p>	<p>We note that there was substantial discussion on this point following the comments received on the first exposure draft of ISAP 4. We also note that the wording has been modified subsequently to reflect the</p>



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	<i>risk adjustment for non-financial risks</i>	<p>possibility of two approaches.</p> <p>We would however like to reiterate our previous suggestion; in particular, that the risk adjustment is measured and assessed separately for gross and reinsured components. The gross risk adjustment should not allow for uncertainty in reinsurance recovery; this is in the reinsurance-related risk adjustment (<i>subject to S118 at the IASB April 2019 TRG AP2</i>).</p> <p>The current wording could imply that non-performance risk could be included in the gross insurance contract risk adjustment.</p> <p>The discussion in the IASB April 2019 TRG AP2 (paragraph S119) could also be reflected here. We understand that this clarifies that non-performance risk should not be allowed for in the determination of the reinsurance risk adjustment.</p>
2.6.13g	<p>We refer to the text:</p> <p><i>When advising on the confidence level disclosure required by IFRS 17, where risk adjustment for non-financial risks has not been determined using a confidence level approach, consider:</i></p> <p><i>The ability to diversify non-financial risks over the entity's consolidated business ...</i></p>	<p>We would agree that it is appropriate for the ISAP to mention the ability to diversify non-financial risks over the entity's consolidated business.</p> <p>However, it may be helpful to include this elsewhere in the ISAP as it is not only relevant to the confidence level disclosure.</p>
2.6.14	<p>We refer to the text:</p> <p><i>Aggregation and Contractual Service Margin (CSM) – The actuary should treat the</i></p>	<p>We would suggest that it could be better to cover aggregation and CSM separately. For example, if an entity were using the Premium Allocation Approach (PAA), then only the aggregation aspects would be</p>



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	<i>processes of: ...</i>	relevant.
2.7	We refer to the text: <i>The Premium Allocation Approach (PAA) – When advising the principal or the entity in relation to the use of the PAA for a group of insurance contracts, the actuary should:</i>	As this refers to ‘group of insurance contracts’ for the PAA, it may be helpful to clarify that this also applies to reinsurance held. <i>This also applies to content on the General Measurement Approach (GMA).</i>
2.7.2	We refer to the text: <i>Be aware of whether the entity has chosen to recognize insurance acquisition cash flows as expenses when it incurs those costs and determine the liability in accordance with the entity’s choice; and</i>	Paragraph 2.7.2 relates to a specific simplification in the IFRS 17 standard (59(a)), where preparers can elect to recognise acquisition costs as they are incurred; (only applicable where the PAA is immediately eligible for that group – i.e. all contracts in the group have a coverage period of less than 12 months). We note that this simplification is considered but other simplifications available under the PAA are not explicitly noted, e.g. discounting on LIC (IFRS 17.59(b)) or discounting on the LRC (IFRS 17.56). As a result, there is undue emphasis on the acquisition costs simplification, and we suggest this paragraph could be removed. Alternatively, paragraph 2.6.12 (relating to acquisition costs) could be modified slightly to consider recognition as well as allocation of acquisition costs.
2.8	We refer to the text: <i>The Variable Fee Approach (VFA) – In using the VFA, the actuary should apply the</i>	As we noted previously, our view is that the section on the Variable Fee Approach (VFA) is quite limited; for example, it does not address the implications for the



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	<i>guidance in paragraph, except for 2.6.6. (Reinsurance Contracts Held) and 2.6.7. (Reinsurance Contracts Issued)</i>	subsequent measurement CSM. We note that IFRS 17 details how the CSM should be measured under the VFA, and that text within 2.6.14 is applicable to both the VFA and GMA. However, in our view it would be useful for the ISAP to note that the VFA is very similar to the GMA, except in detailed aspects of how the CSM is unlocked over time.
2.9.2	We refer to the text: <i>If the actuary becomes aware that presentations and/or disclosures are incorrect or inappropriate, the actuary should discuss these issues with the principal and disclose any concerns in the report.</i>	Our view is that this section could imply that the actuary oversees the entirety of the accounts. This is not usually the actuary's role, and so the scope of this reporting could be stated as specifically in relation to the services provided.

Comments on specific definitions in the Exposure Draft of the updated Glossary

Note that only the proposed revisions are open for comment

Defined Term	Change proposed to the definition (markup preferred)	Reason the change is needed (can be kept very brief or left blank if obvious from the change)
	We note that the Premium Allocation Approach (PAA) is referred to in the Glossary, but it does not appear as an entry in its own right.	The PAA is not defined, although the GMA and FVA are included.