May 25, 2018

Actuarial Standards Board (ASB)
1850 M Street NW, Suite 300
Washington, DC 20036
Via email to: comments@actuary.org

Re: Review of *International Standard of Actuarial Practice 4—IFRS 17 Insurance Contracts* Exposure Draft

On behalf of the Financial Reporting Committee (FRC) of the American Academy of Actuaries,[1] I appreciate the opportunity to provide comments for the Actuarial Standards Board's (ASB) consideration on the exposure draft of the proposed model International Standard of Actuarial Practice 4 (ISAP 4) *IFRS 17 Insurance Contracts*, prepared by the ISAP 4 Task Force of the Actuarial Standards Committee of the International Actuarial Association (IAA). The following comments are relevant should this draft model standard be adopted by IAA member associations.

The FRC has been following the International Accounting Standards Board (IASB) insurance contract accounting project since its inception; many of its current members have followed the project for over 10 years. As such, we have observed the evolution of the project and the final issuance of the standard in May 2017. Given the ASB's role in representing the views of the U.S. actuarial profession on IAA model professional standards, we are providing these comments to you and are posting them on the Academy's website.

<u>General Comments</u>

There was a split among FRC members in their views of whether this was the right time for the IAA to produce an ISAP. Several members expressed the view that generally a standard of practice codifies actual practice. Given the recentness of IFRS 17 and lack of practice prior to implementation of the standard, they felt the ISAP is before its time.

[1] The American Academy of Actuaries is a 19,000+ member professional association whose mission is to serve the public and the U.S. actuarial profession. For more than 50 years, the Academy has assisted public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.

Instead it was suggested the IAA should first focus on finalizing the International Actuarial Note on IFRS 17.

The contrary viewpoint in the FRC was that a short and minimal standard, such as the proposed standard, is necessary to set limited boundaries to aid compliance with IFRS 17. These boundaries would document essential considerations to be made by practicing actuaries and limitations, but not do so in a way that would inhibit the evolution of practice under this new financial reporting standard.

Either way, we expect this ISAP will need to evolve as practice emerges through the implementation of IFRS 17 and an updated version will be needed soon after IFRS 17 becomes effective.

The Role of the Actuary

The model standard as written is not clear about the various roles that the actuary can have in an IFRS 17 assignment. A brief mention of the role is in the introduction (page iv) but not in the model standard itself. As a result, that colors the interpretation of what is written within the model standard. The roles that the actuary may have are as a company employee, consultant, regulator, or employee of an auditing firm. Assignments could range from an initial conversion to IFRS 17, ongoing preparation of inputs to financial statements to some type of back-end opinion that may be requested by management or some regulator on the reasonability of certain actuarially determined portions of the resulting financial statements. The actuary may be part of a team that has a complete view of the entire financial statement or may just be preparing a component part.

Within paragraph 1.2, there is an acknowledgement that if an actuary has a different role, the actuary should apply the standard as relevant. But this alternative role may be more prevalent than the model standard implies, which is that an actuary always works on the entirety of the company rather than on a segment or individual line and/or account.

Relevancy

The draft model standard lists many items that aren't relevant in all cases or all assignments. There should be mention of "where applicable/relevant and material" in many of the lists contained within ISAP 4.

Cat bonds

There is no mention of Cat bonds, which are scoped into IFRS 17 as insurance contracts from the perspective of the bond buyer. We would recommend there be some coverage of this topic.

Business combinations

There is no mention of the treatment for claim liabilities acquired via a business combination. This is a topic that the IAA should consider including in the ISAP.

Transition guidance

There is no mention in the draft model ISAP of the actuary's responsibilities for financial reporting under the transition guidance requiring retroactive application, and whether that means that IFRS 17 must be applied retroactively for past purchases (where there are still outstanding liabilities from the acquired entity).

Actuary's report

There are several references to the "actuary's report" within the exposure draft. We take this to mean the format in which any results are presented but it is not defined in the standard. We would recommend the term "communication" be used instead as defined in ISAP 1, page 11. We believe this would better represent the various roles of an actuary in implementing IFRS 17.

Specific Comments by Paragraph Number

2.1 and 2.2—The paragraphs pull in references to auditing standards and auditor's materiality. While knowledge of such is helpful in an assignment involving IFRS 17, is it appropriate to incorporate it so absolutely? It would be better to have a section on interaction with the auditor.

In the U.S. actuarial standards of practice (ASOPs), in general, there is less specificity on materiality and it is not tied it to the auditor's materiality as the purpose may or may not be the same as the actuary's materiality. It may not be appropriate to link the company actuary's materiality to the auditor's materiality, particularly without reference to a type of assignment. Generally the auditor's materiality will not be available to a preparing actuary for independence reasons.

2.1—The words "where applicable/relevant" should be added before the colon, as not all the items are relevant for all assignments (e.g., the evaluation of claim liabilities from policies written decades ago; the current risk appetite is of limited relevance except possibly for the risk adjustment where that is within the scope of the assignment). In particular, items 2.1.b (risk appetite) and 2.1.c (products and operations) are not always relevant to certain assignments dealing with runoff liabilities, or are only relevant to a limited degree.

2.2, 2.3—These paragraphs should be in ISAP 1, as they don't seem to be specific to IFRS 17.

2.4—ISAP 1 paragraphs 2.7-2.8 require the actuary to always have an opinion on whether they support an assumption applied in their analysis, or state that they had insufficient resources or expertise to evaluate the assumption. There is no option to just state reliance on the other assumption where that is part of their assignment. There should be an option to just state such reliance.

2.4—The last sentence of this paragraph seems to require the actuary to evaluate past processes for items that may be viewed as accounting decisions. That is more of an accounting requirement than an actuarial requirement.

2.5—The reference to ISAP 1 paragraphs 2.7-2.8 appears to require the actuary to have a view on what is an application decision of IFRS 17 (i.e., whether the general measurement approach or Premium Allocation Approach (PAA) applies) rather than solely an actuarial decision. This is similar to requiring the actuary to have an opinion on risk transfer under U.S. generally accepted accounting principles (GAAP). The actuary may be requested to provide the quantitative evidence, but the final application of the accounting standard will likely be the decision of others.

2.6.1—What is an "actuarial assumption"? Why not just say "assumptions"?

2.6.1.a—The mention of considering disaggregation into separate coverages should mention some criteria that would help guide that consideration, such as data volume/credibility and whether such disaggregation is likely to materially impact the final aggregate result. Disaggregation is not always worth the effort and may not always be helpful.

2.6.1.b—This section seems to be short-sighted and could be stated as a positive. Rather than "Be aware," consider saying, "When incorporating assumptions into IFRS modeling, particularly related to pricing, consider the consistency of the assumption with IFRS 17 requirements…"

2.6.1.f—Anti-selection is not always relevant to the assignment. (E.g., the evaluation of runoff claim liabilities.)

2.6.2—Updating the process used to update a "recommended assumption" seems awkward for property and casualty (P&C), as P&C actuaries generally recommend estimates and not individual assumptions. The process to update assumptions is usually just part of updating the accounting estimate, so if updating an accounting policy is an issue then the standard should point out where this could arise.

2.6.3—The last part of this paragraph states that the actuary "should consider relevant factors including the following:..." The words "including the following" says that all the following items must be considered, but not all are always relevant. For example, "the way the contract was sold" (2.6.2.b) may not be relevant for a runoff book. We would suggest adding the word "where" before "relevant."

2.6.5—We would suggest adding "or when producing cash flow estimates." The current wording only addresses the situation when an actuary provides advice on another's calculation, as opposed to producing a recommended estimate themselves.

2.6.5—The phrase "including the following" should be qualified by saying "when relevant and material."

2.6.5.b—The "likelihood of realization of business plans" may not be a material consideration for the runoff of short-duration policies.

2.6.7—The phrase "Entity Discretion" is unclear from the P&C perspective. This is alluding to policyholder dividends, but more clarification would be helpful.

2.6.7.e—This paragraph should probably include “relevant laws and regulations,” as these may not be included in the term “rulings.”

2.6.8.a and b—These aren’t IFRS 17-specific but are generic guidance on ceded reinsurance estimation.

2.6.8.c—Where it says “consider relevant circumstances such as,” not all the items in the following list are relevant to P&C in all cases. Hence add “where relevant and material.”

2.6.9—The authors should check whether IFRS 17 really wants you to anticipate future changes in FX, and in what cases that is required. We do not believe this paragraph is accurately reflecting IFRS 17.

2.6.11—The phrase “should replicate” implies greater precision than we see when providing estimates. Do the authors really mean to apply that high a standard for an estimate?

2.6.12—This should also say “or when producing a recommended estimate for the risk adjustment,” as the current wording implies that the client is doing the estimation and not the actuary.

2.6.12.b—There are an infinite number of “non-financial risks” if one wants to be excessively granular. What is this really asking? As worded, this may be an impossible task.

2.6.12.b.i—What is “compensation risk”? Is this getting at the risk adjustment that compensates the insurer for the risk?

2.6.12.c.ii—We believe this paragraph is misinterpreting IFRS 17. You are required to define portfolios for contracts “subject to similar risks and managed together,” but this doesn’t preclude portfolios that are managed separately but have similar risks. For example, one portfolio could be auto insurance in the American Midwest (managed by one region) with another being auto insurance in the Pacific coast (managed by another region). They might have similar risks, despite being managed by different people. Hence there is no requirement per se that the risk methodology should reflect risk differences between portfolios, as such differences may not exist.

Note that IFRS17 also allows calculation of items on a more aggregated basis and then allocate to group. This wording doesn’t seem to reflect that possibility.

2.6.12.f—This wording implies that you would calculate the gross and ceded to get the net. In many cases it is easier (and produces a better estimate) to calculate the gross and net, and then back into the ceded. The wording should allow for calculating the gross and net and backing into the ceded.

2.6.13—This paragraph doesn’t allow for an actuary who is only working on a segment of the total, relying on others for the level of aggregation/disaggregation. This wording forces the actuary to have an opinion on items outside the scope of the actuary’s work.

2.6.14.a-b—This is not germane (and is somewhat misleading) for a company with all its contracts under PAA that has acquired a company with long-tail claim liabilities. The entity's policy (if all under PAA) is not relevant to the acquired long-tail claim liabilities.

2.7.1—The accounting for deferred acquisition costs is typically not an actuarial exercise for a P&C company, hence this paragraph is not always (if ever) relevant to an actuary doing work under PAA.

The phrase "Be aware" is also used in 2.7.1. Consider rephrasing as, "Consider the entity's recognition election for insurance acquisition cash flows as expenses and determine the liability consistently with this election."

2.7.2.a—The term "expenses" in this paragraph may be misleading, as IFRS 17 includes claim payments in its term "expenses." Hence this needs clarification.

2.7.2.a—It is not clear what is meant by the term "incurred insurance revenue". Perhaps this should be "recognized insurance revenue"?

2.7.3—Guidance to "Review regularly" something may not be consistent with the actuary's assignment.

2.9—Each of the items in 2.9 seem rather all-inclusive. In reality, we are not sure that these have the time line of the actuarial work in comparison with the financial statement in the appropriate order.

2.9.1—The term "all" in this paragraph is problematic, as it is in any standard, as it can be an impossible task to completely provide "all" information, but the "all" criteria can significantly increase litigation risk. This paragraph also doesn't provide much guidance to an actuary.

2.9.2—Is the actuary's report always prepared after the completion of the financial statement? Many times it will be feeding the financial statement, so it will be available before the financial statement and not known whether its work is interpreted correctly.

Also, it is unclear which presentations this paragraph refers to—only those involved with the assignment? Further, it is not clear why this paragraph is in the past tense—some copy-editing may be in order. Finally, the FRC wonders whether this might not be better covered by ISAP 1 instead.

2.10—Are all the listed items always relevant? If not, add "where relevant."

3.1—This is the likely place to define the report/communication based on our earlier comments.

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Thank you for this opportunity to provide our views on the current draft of a proposed model actuarial standard of practice, *IFRS 17 Insurance Contracts*. If you have any questions or would like to discuss this letter in more detail, please contact Nikhail Nigam, the Academy's policy analyst for risk management and financial reporting issues, at 202-223-8196 or nigam@actuary.org.

Sincerely,

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