



## ISAP 4

# International Standard of Actuarial Practice 4 IFRS 17 Insurance Contracts (ISAP 4)

**NOTE:** Defined terms in this Exposure Draft are marked in blue coloured text with dotted underline. IFRS 17 terms are marked in green coloured text with double underline. The defined terms in the approved final ISAP will have hyperlinks to the relevant definition in the Glossary. Please note that the hyperlinks have not been created in this Exposure Draft.

Developed by the ISAP 4 Task Force of the  
Actuarial Standards Committee  
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## Preface

**~~This International Standard of Actuarial Practice (ISAP) is a model for actuarial standard-setting bodies to consider.~~**

~~The International Actuarial Association (IAA) encourages relevant actuarial standard-setting bodies to maintain a standard or set of standards that is substantially consistent with this ISAP to the extent that the content of this ISAP is appropriate for actuaries in their jurisdiction. This can be achieved in many ways, including:~~

- ~~• Adopting this ISAP as a standard with only the modifications in the Drafting Notes;~~
- ~~• Customizing this ISAP by revising the text of the ISAP to the extent deemed appropriate by the standard-setting body while ensuring that the resulting standard or set of standards is substantially consistent with this ISAP;~~
- ~~• Endorsing this ISAP by declaring that this ISAP is appropriate for use in certain clearly defined circumstances;~~
- ~~• Modifying existing standards to obtain substantial consistency with this ISAP; or~~
- ~~• Confirming that existing standards are already substantially consistent with this ISAP.~~

~~A standard or set of standards that is promulgated by a standard-setting body may be considered to be substantially consistent with this ISAP if:~~

- ~~• There are no material gaps in the standard(s) in respect of the principles set out in this ISAP; and~~
- ~~• The standard or set of standards does not contradict this ISAP.~~

~~Local jurisdictions may adopt variants of IFRS 17, and in that case a local actuarial standard-setter may need to adjust ISAP 4 accordingly.~~

~~If an actuarial standard-setting body wishes to adopt or endorse this ISAP, it is essential to ensure that existing standards are substantially consistent with ISAP 1 and ISAP 1A as this ISAP relies upon ISAP 1 and ISAP 1A in many respects. Likewise, any customization of this ISAP, or modification of existing standards to obtain substantial consistency with this ISAP, should recognize the important fact that this ISAP relies upon ISAP 1 and ISAP 1A in many respects.~~

~~If this ISAP is translated for the purposes of adoption, the adopting body should select three verbs that embody the concepts of “must”, “should”, and “may”, as described in paragraph 1.6. Language of ISAP 1, even if such verbs are not the literal translation of “must”, “should”, and “may”.~~

**~~This ISAP is a model standard of actuarial practice and, as such, is not binding on any actuary.~~**

~~This ISAP was adopted by the IAA Council in [mmm yyyy].~~

~~*[Drafting Notes: When an actuarial standard-setting organization adopts this standard, it should:*~~

- ~~1. Replace “ISAP” throughout the document with the local standard name, if applicable;~~
- ~~2. Modify references to ISAP 1 and ISAP 1A in paragraphs 1.3., 2.1., 2.2.2., 2.3., 2.4., 2.5., 2.6.13., and 3.1. to point to the local standard(s) that are substantially consistent with ISAP 1 and ISAP 1A, rather than referring to ISAP 1 or ISAP 1A directly, if appropriate;~~
- ~~3. Choose the appropriate phrase and date in paragraph 1.7.;~~

- ~~4. Review this standard for, and resolve, any conflicts with the local [law](#) and code of professional conduct; and~~
- ~~5. Delete this preface (including these drafting notes) and the footnote associated with paragraph 1.7.]~~

### Introduction

The International Accounting Standards Board (IASB) issued International Financial Reporting Standard 17 ([IFRS 17](#)) Insurance Contracts in May 2017.

This International Standard of Actuarial Practice (ISAP) provides guidance to [actuaries](#) when performing [actuarial services](#) in connection with [IFRS 17](#).

As described by the IASB in their Project Summary of May 2017, [IFRS 17](#) ‘requires a company that issues [insurance contracts](#) to report them on the balance sheet as the total of:

- a. The [fulfilment cash flows](#) – the current estimate of amounts that the insurer expects to collect from premiums and pay out for claims, benefits and expenses, including an adjustment for the timing and risk of those cash flows; and
- b. The [contractual service margin \(CSM\)](#) – the expected profit for providing future insurance coverage (i.e. unearned profit).’

An [entity](#) which reports financial statements under IFRS is responsible for all the information reported in its [International Financial Reporting Standards \(IFRS\)](#) financial statements. This means it is responsible for identification, recognition and derecognition and classification of contracts, the choice of measurement approach and assumptions, the measurement calculations and disclosures in the [IFRS](#) financial statements.

Nevertheless, [actuaries](#) providing [actuarial services](#) in connection with [IFRS 17](#) may be making decisions for the [entity](#), advising the [entity](#) on decisions, [ensuring regulation is complied with](#), carrying out the calculations required or some combination of these.

This ISAP is intended to:

- Facilitate convergence in standards of actuarial practice in connection with [IFRS 17](#) within and across jurisdictions;
- Increase public confidence in [actuarial services](#) provided in connection with [IFRS 17](#); and
- Demonstrate the [IAA](#)’s commitment to support the work of the IASB in achieving high quality, transparent and comparable financial reporting internationally, as envisaged by the Memorandum of Understanding between the [IAA](#) and the IASB.

**Section 1. General**

- 1.1. Purpose** – This ISAP provides guidance to [actuaries](#) when performing [actuarial services](#) in connection with [IFRS 17](#). Its purpose is to increase [intended users](#)' confidence that:
- [Actuarial services](#) are carried out professionally, ~~and~~ with due care [and comply with regulation](#);
  - The results are relevant to their needs, are presented clearly and understandably, and are complete; and
  - The assumptions and methodology (including [models](#) and modelling techniques) used are disclosed appropriately.
- 1.2. 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. [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) should apply the guidance in this ISAP to the extent relevant to the assignment.
- 1.3. Relationship to ISAP 1 and ISAP 1A** – Compliance with [ISAP 1](#) and [ISAP 1A](#) is a prerequisite to compliance with this ISAP. References in [ISAP 1](#) and [ISAP 1A](#) to “this ISAP” should be interpreted as applying equally to ISAP 4, where appropriate.
- 1.4. Relationship to IFRSs** – This ISAP relates to the content of [IFRS 17](#) and other [IFRSs](#), including any interpretations from the International Financial Reporting Interpretations Committee or the Standing Interpretations Committee thereon (IFRIC), as issued through MONTH 20XX [date of final consultation on ISAP 4]. The guidance in this ISAP complements the guidance in [IFRS 17](#), which is not repeated in this ISAP.
- 1.5. Defined Terms** – This ISAP uses various terms whose specific meanings are defined in the Glossary. These terms are highlighted in the text with a dashed underscore and in blue, which is a hyperlink to the definition (e.g., [actuary](#)).
- This ISAP also uses key terms from [IFRS 17](#), in which case they have the meaning as used in [IFRS 17](#). These terms are highlighted in the text with a double underscore and in green (e.g., [insurance contract](#)).
- 1.6. Cross References** – If [IFRS 17](#), or any other [IFRS](#) referenced in this ISAP, is subsequently amended, restated, revoked or replaced by the IASB, or interpreted by IFRIC after MONTH 20XX, the [actuary](#) should consider the extent to which guidance in this ISAP is still applicable and appropriate.
- 1.7. Effective Date** – This ISAP is effective for {[actuarial services](#) performed/[actuarial services](#) commenced/[actuarial services](#) performed with respect to an [IFRS](#) financial statements for a reporting period ending}<sup>1</sup> on or after [Date]

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<sup>1</sup> [Phrase to be selected and date to be inserted by standard-setter adopting or endorsing this ISAP.].

## Section 2. Appropriate Practices

- 2.1. Relevant Knowledge Requirements** – In applying [ISAP.1](#) paragraph 2.2. Knowledge of Relevant Circumstances, the [actuary](#) should have or obtain sufficient knowledge and understanding of information necessary to perform the assignment, such as:
- a. [IFRS.17](#), applicable sections of other relevant [IFRSs](#) (e.g., IFRS 13 when determining Fair Value), the [entity](#)'s [accounting policies](#) and the relevant processes that are applied in the preparation of [IFRS](#) financial statements;
  - b. The [entity](#)'s appetite for any risk that has an impact on the measurement under [IFRS.17](#);
  - c. The [entity](#)'s products and operations;
  - d. The methodologies and assumptions used by the [entity](#) in other relevant contexts and the rationale for any differences;
  - e. How [law](#) affects the application of [IFRS.17](#); and
  - f. The relevant auditing standards.
- 2.2. Materiality** – The [actuary](#) should understand the distinction between materiality with respect to the [actuarial services](#), the preparation of [IFRS](#) financial statements and the auditing of those financial statements.
- 2.2.1. When appropriate for the [work](#), the [actuary](#) should seek guidance from the [principal](#) or the [entity](#) regarding materiality.
  - 2.2.2. In applying [ISAP.1](#) paragraph 2.4. Materiality, the [actuary](#)'s threshold of materiality with respect to the [actuarial services](#) should not be greater than the [entity](#)'s threshold or the auditor's threshold of materiality with respect to the preparation of [IFRS](#) financial statements.
  - 2.2.3. In all following paragraphs of this ISAP, any use of “material” or “materiality” is with respect to the [actuarial services](#).
- 2.3. Proportionality** – In applying [ISAP.1](#) paragraph 1.5. Reasonable Judgment, and in particular paragraph 1.5.2., the [actuary](#) should take materiality into account. The degree of refinement in specific assumptions or methods recommended by the [actuary](#) should be proportionate to their possible impact on the results of the [actuarial services](#).
- 2.4. Identification, Separation, Recognition, Derecognition and Modification** – The [actuary](#) should treat the processes of:
- a. Identification of [insurance contracts](#);
  - b. Separation of components from an [insurance contract](#);
  - c. Recognition and derecognition of [insurance contracts](#);
  - ~~e~~.d. [Determination of the level of aggregation](#); and
  - ~~e~~.e. Determination of whether an [insurance contract](#) modification is a change that is to be treated as derecognition of the contract and recognition of the modified contract as a new contract, or whether the modification is to be treated as a change in estimates of [fulfilment cash flows](#)
- as processes to which [ISAP.1](#) paragraphs 2.7. Assumptions and Methodology Set by Actuary or 2.8. Assumptions and Methodology Prescribed applies.

The [actuary](#) should disclose in the [actuary's report](#) changes in the above processes, including the rationale for the changes and their impact.

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- 2.5. Measurement Approach** – The [actuary](#) should treat the processes of selecting the appropriate measurement approach to be applied to each [group of insurance contracts](#), whether it is the [general measurement approach](#), the [premium allocation approach \(PAA\)](#) or the [variable fee approach](#), as processes to which [ISAP.1](#) paragraphs 2.7. Assumptions and Methodology Set by Actuary or 2.8. Assumptions and Methodology Prescribed applies.

The [actuary](#) should disclose in the [actuary's report](#) changes in the above processes, the rationale for the changes and their impact.

## 2.6. The General Measurement Approach

- 2.6.1. **General approach for selection of assumptions** – When advising the [principal](#) or the [entity](#) on actuarial assumptions, the [actuary](#) should:

- a. For the purpose of setting assumptions, consider disaggregating [insurance contracts](#) into [separate](#) coverages with similar risks based on the nature of the insurance obligation;
- b. Be aware that current pricing assumptions may not be appropriate for [IFRS.17](#) purposes;
- c. Make links as necessary to ensure consistency between assumptions (e.g., assumptions related to option exercise patterns should be linked to the economic scenarios);
- d. Consider the potential asymmetrical distribution of the current estimates (e.g., assumptions to deal with extreme events like tail events or options and guarantees that are triggered by market conditions);
- e. Consider the use of credibility techniques when combining information from various sources or time periods; and
- f. Consider [anti-selection](#) and its effect over time.

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- 2.6.2. **Process for Updating Assumptions** – If the [actuary](#) considers it appropriate to change the process [and / or methods](#) 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 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

The [actuary](#) should disclose in the [actuary's report](#) changes in the above processes, the rationale for the changes and their impact.

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- 2.6.3. **Insurance Risks** – When advising the [principal](#) or the [entity](#) on assumptions to measure [insurance risks](#), the [actuary](#) should consider relevant factors including the following:

- a. Characteristics of the [insurance risk](#);
- b. Characteristics of the policyholder and the way the contract was sold;
- c. Past experience of incurred claims including patterns of delays in reporting and payment and the relevance to expected future experience;
- d. Adjustments to past experience of incurred claims, including claim inflation;
- e. Allowance for extreme events;



- f. Practices of the entity; and
  - g. External factors, such as secular trends and seasonal variations, and changes in the legal, economic, legislative, regulatory, supervisory, demographic, technological and social environments.
- 2.6.4. Options – When advising the principal or the entity on assumptions for expected option exercise patterns, the actuary should consider relevant factors and changes therein including the following:
- a. Sophistication of the policyholder, as well as the relative advantages, to the policyholder, of exercising any options;
  - b. Characteristics of how the insurance contracts are sold and serviced;
  - c. Significant scheduled changes in benefits;
  - d. Any short-term spikes in cancellation rates created by the exercise of certain options; and
  - e. External factors such as the market conditions, legal, economic, legislative, regulatory, supervisory, demographic, technological and social environments.
- 2.6.5. Maintenance Expenses – When advising the principal or the entity on the projection of cash flows for maintenance expenses, the actuary should consider relevant factors including the following:
- a. The entity's cost-accounting and expense allocation policies;
  - b. Expenses expected to arise from fulfilling obligations existing on the measurement date. This estimate should consider the entity's past expenses and ~~the likelihood of the realization~~ be consistent of with business plans; and
  - c. Any outsourcing arrangements.
- 2.6.6. Contracts with Participation Features or Other Variable Cash Flows - When advising the principal or the entity, the actuary should:
- a. Select a discount rate used to calculate the present value of the cash flows to measure the fulfilment cash flows that reflect the expected returns anticipated in the projection of the future cash flows. Returns on assets should be projected using prospective expectations consistent with ~~expected future economic conditions~~ observable current market prices; and
  - b. Consider the associated impact, if any, on the estimates of future cash flows, the risk adjustment for non-financial risks and the discount rate in the projection, when the cash flows depending on the underlying items have a floor or a cap.
- 2.6.7. Entity Discretion – When advising the principal or the entity on assumptions to reflect entity discretion, the actuary should take into account expectations or limitations that may arise from sources such as:
- a. The entity's marketing and promotional materials;
  - b. The entity's past practices insofar as relevant for the future;
  - c. The entity's current policy;
  - d. Market practices; and

- e. Rulings of relevant authorities.
- 2.6.8. **Reinsurance** – When advising the **principal** or the **entity**, on the measurement of **reinsurance contracts**, the **actuary** should:
- a. When estimating amounts recoverable under multiple reinsurance arrangements, consider the order of reinsurance recovery;
  - b. When estimating non-recoverable amounts, consider the financial condition of the reinsurer and the extent to which default by one reinsurer may affect the amounts recoverable from other reinsurers;
  - c. When estimating the **fulfilment cash flows** of a **reinsurance contract** issued by the **entity**, consider relevant circumstances such as:
    - i. The expected behaviour with respect to the available options of both the policyholders of the underlying **insurance contracts** and all ceding issuers, including retrocessionaires, if any;
    - ii. The underwriting and management practices, including the underwriting for facultative placements, and the claim management processes of the ceding issuers;
    - iii. The impact of reinstatements; and
    - iv. Default by ceding issuers, including retrocessionaires, if any.
  - d. When projecting cash flows over future periods, consider the extent to which the issuer of the underlying **insurance contract** and each reinsurer exercise their control over recapture, cancellation or commutation to their advantage.
- 2.6.9. **Currency Exchange** – When advising the **principal** or the **entity** on the estimation of the **fulfilment cash flows** in multiple currencies, the **actuary** should reflect the expected future changes in currency exchange rates and the uncertainty arising from currency fluctuations.
- 2.6.10. **Discount Rates** – When advising the **principal** or the **entity** on discount rates, the **actuary** should:
- a. When deriving the discount rates applied to cash flows beyond the period for which observable market data is available, **use extrapolation techniques that maximize the use of observable market data and are consistent with economic expectation**~~consider how current rates would be expected to evolve over time;~~
  - b. When deriving the discount rates applied to cash flows of **insurance contracts**, which ~~depend vary based~~ on the returns of **underlying items** ~~consider either using risk neutral discount rates combined with a risk neutral projection of the underlying item or real world discount rates combined with a real world projection of the underlying item;~~ **the entity's invested assets, consider the entity's investment policy, taking into account the entity's communications to various stakeholders and with due regard for anticipated policyholder behaviour;** and
  - c. When deriving the illiquidity adjustment for the discount rate, consider:
    - i. Approaches that are robust and that should be able to be applied reliably over time and under a variety of market conditions; and

- ii. Available market data (e.g., credit default swap spreads) when deducting a credit or default allowance from observed asset yield rates.
- 2.6.11. **Insurance Acquisition Cash Flows** – The actuary should be satisfied that the allocation of insurance acquisition cash flows is made on a consistent basis to each portfolio of insurance contracts. The insurance acquisition cash flows should replicate actual acquisition costs.
- 2.6.12. **Risk Adjustment for Non-Financial Risks** – When advising the principal or the entity on the risk adjustment for non-financial risks, the actuary should:
- a. Identify the non-financial risks inherent in the insurance contracts;
  - b. In assessing what the entity requires as compensation for bearing the non-financial risks:
    - i. Take into account any diversification benefit the entity includes in its compensation risk; and
    - ii. Consider sources of relevant information such as the entity's capital management, risk management and pricing policies.
  - c. Select a methodology that:
    - i. Uses assumptions that are consistent with those used in the determination of the corresponding estimates of future cash flows; and
    - ii. Is granular enough to reflect the risk differences between the portfolios of insurance contracts.
  - d. Make appropriate allowance for mechanisms that result in risk being passed to the policyholder (e.g., contracts with participation or adjustment features);
  - e. Assess the uncertainty caused by the potential of non-performance by reinsurers within the risk adjustment for non-financial risks;
  - f. Consider whether the difference between the total of the calculated gross risk adjustments for non-financial risks and the total of the ceded risk adjustment for non-financial risks fairly reflects the compensation that the entity requires for its net of reinsurance exposure; and
  - g. When advising on the determination of the confidence level disclosure corresponding to the risk adjustment, required by IFRS 17, where risk adjustment for non-financial risks has been determined using a technique other than a specified confidence level, consider:
    - i. The entity's ability to diversify non-financial risks over the total business; and
    - ii. The inherent uncertainty in the translation to a confidence level and the need to disclose such uncertainty in the actuary's report.
- 2.6.13. **Aggregation and Contractual Service Margin (CSM)** – The actuary should treat the processes of:
- a. Identification of portfolios of insurance contracts;
  - b. Allocation of individual insurance contracts into portfolios, and each portfolio into groups of insurance contracts;
  - c. Treatment of loss component on onerous contracts; and

- d. Determination of the [coverage units](#) as processes to which [ISAP.1](#) paragraphs 2.7. Assumptions and Methodology Set by Actuary or 2.8. Assumptions and Methodology Prescribed applies. The [actuary](#) should disclose in the [actuary's report](#) changes in the above processes, the rationale for the changes and their impact.
- 2.6.14. **Acquisition of Insurance Contracts by Transfers or Business Combinations** – When advising the [principal](#) or the [entity](#), the [actuary](#) should:
- Follow procedures that are consistent with those for [insurance contracts](#) issued; and
  - For [liabilities for incurred claims](#), follow the [entity's](#) policy regarding deferral of profit, recognize any loss immediately and amortize any excess of consideration over the [fulfilment cash flows](#), akin to a [CSM](#).
- 2.7. The Premium Allocation Approach** – When advising the [principal](#) or the [entity](#) in relation to the use of the [PAA](#) for a [group of insurance contracts](#), the [actuary](#) should:
- 2.7.1. Be aware of whether the [entity](#) has opted to recognize [insurance acquisition cash flows](#) as expenses and determine the liability consistently with the [entity's](#) approach;
- 2.7.2. If the [coverage period](#) is longer than one year, assess whether the [PAA](#) is a reasonable simplification of the [general measurement approach](#), by considering whether:
- The pattern of expected incurred insurance service expenses, plus the release of the [risk adjustment for non-financial risks](#), plus the release of the [CSM](#) under the [general measurement approach](#) is materially different from the expected timing of incurred insurance revenue under the [PAA](#);
  - There is a reasonable expectation that differences between the timing of cash flows under the [general measurement approach](#) and the timing of incurred insurance service expenses under the [PAA](#) will result in materially different adjustments for the time value of money; and
  - There is a reasonable expectation that future assumption changes under the [general measurement approach](#) in response to emerging experience will render the simplification invalid in future.
- 2.7.3. Review regularly the [group of insurance contracts](#) to determine if it is or has become [onerous](#) and advise the [principal](#) or the [entity](#) accordingly.
- 2.8. The Variable Fee Approach** – In using the [variable fee approach](#), the [actuary](#) should determine the [fulfilment cash flows](#) in accordance with guidance in paragraph 2.6., except for 2.6.8. (Reinsurance).
- 2.9. Financial Statement Presentation and Disclosure**
- 2.9.1. Where the terms of the assignment are such that the information provided by the [actuary](#) may be used in financial statement presentation and disclosure, the [actuary](#) should provide all related information needed to comply with the relevant presentation and disclosure requirements of [IFRS 17](#) and the [entity's accounting policies](#).
- 2.9.2. If the [actuary](#) had become aware that presentations and/or disclosures are incorrect or

inappropriate, the [actuary](#) should disclose that in the [actuary's report](#).

- 2.9.3. In providing advice on the disclosures of reconciliations where the order of calculations alter the information disclosed, the [actuary](#) should apply a consistent order of calculation across all reconciliations and from period to period, or disclose any change, its rationale and its impact in the [actuary's report](#).

**2.10. Transition** – When advising the [principal](#) or [entity](#) on whether the [retrospective approach](#) is impracticable, the [actuary](#) should take into consideration relevant factors including:

- a. The availability and integrity of past policy data that are required to determine the [fulfilment cash flows](#) since initial recognition;
- b. The availability and integrity of information on past products;
- c. The availability of sufficient data to determine the initial assumptions and subsequent changes that would have been made over the lifetime of the various [insurance contracts](#);
- d. The method used to adjust past known interest rates to achieve the rates that represent the characteristics of the [insurance contracts](#); and
- e. The difficulty in evaluating the past [risk adjustment for non-financial risks](#) and management discretion without the benefit of hindsight.

### Section 3. Communication

**3.1. Disclosures in the Report** – In addition to complying with [ISAP.1](#) Section 3. Communication and [ISAP.1A](#) Section 3. Communication, the [actuary](#) should disclose:

- 3.1.1. Information regarding a change in assumptions or method, whether arising from a consistent or changed process;
- 3.1.2. The rationale and impact of any changes in approaches, including:
  - a. The identification of [insurance contracts](#), the separation of components, the recognition, derecognition and modification of [insurance contracts](#) (2.4.);
  - b. The determination of the measurement approach (2.5.);
  - c. The assumptions (2.6.2.);
  - d. The identification of [portfolios of insurance contracts](#), the allocation into [groups of insurance contracts](#), the treatment of [loss component](#) and the approach to the determination of [coverage units](#) (2.6.13.); and
  - e. The order of calculation on reconciliations provided for presentation items (2.9.3.).
- 3.1.3. When the [risk adjustment for non-financial risks](#) is determined using a technique other than a specified confidence level, the uncertainty inherent in the translation to a confidence level (2.6.12.g.); and
- 3.1.4. Any concerns about the presentation of any items or of any disclosures ([2.9.22-9](#)).