ISAP 3 – Actuarial Practice under IAS 19 Employee Benefits - Exposure Draft

This document contains the exposure draft of proposed ISAP 3 – Actuarial Practice under IAS 19 Employee Benefits. Please review this exposure draft and determine how you wish to address the issues it covers within your association. Comments (from your organization, your members, or other parties to which you forward these exposure drafts) should be addressed to ISAP3.ED.comments@actuaries.org with "ISAP – IAS 19" in the email header. The comment should make clear if it is a personal response or one representing a particular association, standard-setter, or other entity.

The preferred format for submitting comments is email or an MS Word (or equivalent) attachment. If a markup of the exposure draft is submitted we recommend using the Comment feature liberally, giving reasons for proposing the change. All comments will normally be posted to the International Actuarial Association website identifying the commenter(s). However, in exceptional cases, in response to a request which the IAA Secretariat is satisfied is for a valid reason, comments may be either posted to the website anonymously or withheld from the website.

The deadline for comments to be considered by the drafting committee is 14 March 2014.

This document was approved for exposure by the Actuarial Standards Committee in October 2013.

ASSOCIATION ACTUARIELLE INTERNATIONALE
INTERNATIONAL ACTUARIAL ASSOCIATION

International Standard of Actuarial Practice3 (ISAP 3)

Actuarial Practice under IAS 19 Employee Benefits

NOTE: Defined terms in this Exposure Draft are marked in blue coloured text with dotted 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.

Approved by the IAA Council

[Day Month Year]

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ISAP 3 – Actuarial Practice under IAS 19 Employee Benefits - Exposure Draft
Preface

[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 in paragraphs 1.3, 1.4, 2.2.1, 2.6, 2.6.7, 2.7.1, and 3.1 to point to the local standard(s) that are substantially consistent with ISAP 1, rather than referring to ISAP 1 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.]*

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 consider taking one of the following courses of action, if it has been determined that this ISAP is relevant for actuaries in their jurisdiction:

- Adopting this ISAP as a standard with appropriate modification, where items covered in this ISAP are not currently contained in existing actuarial standards;
- Endorsing this ISAP as a standard as an alternative to existing standards;
- Modifying existing standards to obtain substantial consistency with this ISAP; or
- Confirming that existing standards are already substantially consistent with this ISAP.

Such an adopted standard (rather than this ISAP) applies to those actuaries who are subject to such body's standards, except as otherwise directed by such body (for example with respect to cross-border work).

When this ISAP is translated, 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 not binding upon an actuary unless the actuary states that some or all of the work has been performed in compliance with this ISAP.

This ISAP was adopted by the IAA Council in [month year].

ISAP 3 – Actuarial Practice under IAS 19 Employee Benefits - Exposure Draft

Introduction

This International Standard of Actuarial Practice (ISAP) provides guidance to actuaries when performing actuarial services in connection with International Accounting Standard 19 (IAS 19) Employee Benefits.

The reporting entity is responsible for all the information reported in its IFRS report, including information reported in accordance with IAS 19. This means the reporting entity is responsible for the categorization of employee benefit plans, the choice of actuarial assumptions and methods used to measure employee benefit obligations, and disclosures about employee benefit plans. IAS 19 encourages, but does not require, a reporting entity to involve a qualified actuary in the measurement of all material post-employment benefit obligations. In practice, an actuary may advise on a range of issues arising from the reporting entity's application of IAS 19, including the measurement of short-term, post-employment, termination, or other long-term employee benefits and disclosures in the IFRS report.

This ISAP is intended to:

- Facilitate convergence in actuarial practice in connection with IAS 19 within and across jurisdictions;
- Increase reporting entities' and their auditors' confidence in actuaries' contributions to reporting of employee benefits in accordance with IAS 19;
- Increase public confidence in actuaries' services for IAS 19 purposes; 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 IAS 19. The focus is on actuarial services provided for a reporting entity's preparation of an actual or pro-forma IFRS report. Its purpose is to give intended users confidence that:

- Actuarial services are carried out professionally and with due care, in compliance with IAS 19, and taking into account the reporting entity's accounting policies;
- The results are relevant to their needs, are presented clearly and understandably, and are complete; and
- The assumptions and methodology (including, but not limited to, models and modelling techniques) used are disclosed appropriately.

1.2. Scope – This ISAP provides guidance to actuaries when performing actuarial services in connection with IAS 19. The focus is on services provided for a reporting entity's preparation of an actual or pro-forma IFRS report for any type of employee benefit the reporting entity determines to be covered by IAS 19. An actuary who is performing these actuarial services may be acting in one of several capacities such as an employee, management, director, external adviser, auditor, or supervisory authority of the reporting entity.

1.3. Compliance – There are situations where an actuary may deviate from the guidance of this ISAP but still comply with it:

1.3.1. Law may impose obligations upon an actuary. Compliance with requirements of law that conflict with this ISAP is not a deviation from it.

1.3.2. The actuarial code of professional conduct applicable to the work may conflict with this ISAP. Compliance with requirements of the code that conflict with this ISAP is not a deviation from it.

1.3.3. The actuary may depart from the guidance in this ISAP while still complying with it if the actuary provides, in any report, an appropriate statement with respect to the nature, rationale, and effect of any such departure.

Paragraphs 2.6, 2.8, and 2.9 of ISAP 1 cover the situation where the actuary is directed to use certain assumptions or methodology. The actuary who complies with these paragraphs is not deviating from this ISAP.

1.4. Relationship to ISAP 1 – Any actuary who asserts compliance with this ISAP (as a model standard) must also comply with ISAP 1. References in ISAP 1 to "this ISAP" should be interpreted as applying equally to this ISAP 3, where appropriate.

1.5. Glossary – 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).

1.6. Cross References – This ISAP refers to the content of IAS 19 as amended by the IASB in June 2011. If IAS 19 is amended, restated, revoked, or replaced after June 2011, the actuary should consider the extent to which the guidance in this ISAP remains applicable and appropriate.

Comment [Z1]: To increase would be better wording, it should be used consistently as we can see in the Introduction.

Comment [Z2]: We recommend using numbering instead of bulleting, it makes easier the references.

1.7. Effective Date – This ISAP is effective for {actuarial services performed/actuarial services commenced/actuarial services performed with respect to an IFRS report issued}[1] on or after [Date].

[1] *[Phrase to be selected and date to be inserted by standard setter adopting or endorsing this ISAP.]*.

Section 2. Appropriate Practices

2.1 **Knowledge of Accounting Requirements** – To be confident in performing the actuarial services, the actuary should have or obtain sufficient knowledge and understanding of IAS 19, relevant paragraphs of other IFRSs to which IAS 19 refers, and the reporting entity's relevant accounting policies. The actuary should seek guidance from the principal when:

a. The actuary is uncertain whether another IFRS is relevant to the actuarial services; or

b. The actuary envisions that a specific component of the actuarial services may be subject to alternative interpretations of IAS 19, a relevant paragraph of another IFRS, or a relevant accounting policy.

2.2 **Materiality** – The actuary should differentiate between materiality with respect to the actuarial services and materiality with respect to the IFRS report.

2.2.1 The actuary should be guided by ISAP 1 in assessing materiality with respect to the actuarial services. The principal or reporting entity (not the user of the IFRS report) is the intended user of the actuarial services for this purpose.

2.2.2 The reporting entity is responsible for assessing materiality with respect to the IFRS report. The actuary should seek guidance from the principal or reporting entity, as appropriate for the work, regarding materiality with respect to the IFRS report and take that guidance into account when advising the principal on whether to measure an obligation, the use of refined or approximate actuarial assumptions and methods, and the level of detail for presenting results.

2.2.3 In the remainder of this ISAP, any use of "material" or "materiality" is with respect to the IFRS report unless stated otherwise.

2.3 **Material Errors, Omissions, or Non-conformance** – If, the actuary becomes aware that information used in performing the actuarial services – including information about employees and their dependents or beneficiaries, employee benefit plan provisions and operations, plan assets, the reporting entity's accounting policies, and the reporting entity's categorization of employee benefit plans – contains material errors, omissions, or fails in another material manner to conform to IAS 19, other relevant IFRSs, or the reporting entity's accounting policies, the actuary should inform the principal and seek to resolve the matter. If such a matter is discovered and not resolved in a satisfactory way before the actuary issues the report, the actuary should disclose the matter in the report. This guidance does not impose additional duties beyond the scope of the actuarial services to search for or analyse such errors, omissions, or failures to conform to IFRSs or accounting policies.

2.4 **Constructive Obligations** – The actuary may rely on representations made by the principal regarding the existence and nature of any formal or informal practices that give rise to a constructive obligation. The actuary should disclose reliance on such representations in the report.

If it becomes apparent to the actuary in the course of performing the actuarial services that significant uncertainties exist regarding such representations, the actuary should seek clarification from the principal. If the uncertainty is not resolved in a satisfactory way before the actuary issues the report, the actuary should be guided by paragraph 2.3. This guidance does not impose additional duties beyond the scope of the actuarial services to search for or analyse constructive obligations that go beyond formal plans or agreements.

2.5 **Categorization of Employee Benefit Plan** – The reporting entity is responsible for determining the categorization of its employee benefit plans under IAS 19 as short-term,

Comment [Z3]: We think that the aim here is twofold: emphasizing the exclusive responsibility of the principal while preserving the professional integrity of the actuary. In these terms we would propose the wording "consult with" instead of "seek guidance from". The outcome of the consultations should be disclosed in the report as the responsibility of the principal just as in points 2.4-2.6.

Comment [Z4]: We suggest to use wording reporting entity's relevant accounting policies consistently, consistent wording always enhances usability.

Comment [Z5]: See previous comment on "seek guidance from".

Comment [Z6]: The responsibility of other parties should always be disclosed in the report. The Standard should definitely express this requirement as it does in 2.4.

Inclusion of "The actuary should disclose reliance on such representations in the report." would be beneficial.

defined benefit post-employment, defined contribution post-employment, termination, or other long-term.

2.5.1 The actuary may advise the principal regarding the categorization of an employee benefit plan. When providing such advice, the actuary should exercise professional judgment when an employee benefit plan has characteristics of multiple categories (such as retirement plans that combine elements of defined benefit and defined contribution plans, or employment-related injury benefits that include both medical care and wage replacement).

2.5.2 The actuary should apply the reporting entity's categorization of an employee benefit plan. If it is or becomes apparent to the actuary in the course of performing the actuarial services that such categorization fails in a material manner to conform to IAS 19, the actuary should be guided by paragraph 2.3.

2.5.3 If the actuary is uncertain as to the reporting entity's IAS 19 categorization of an employee benefit plan, the actuary should seek guidance from the principal.

2.6 **Actuarial Assumptions** – The reporting entity is responsible for selecting assumptions that represent the reporting entity's best estimates of the variables that will determine the ultimate costs of its employee benefits. The actuary may advise the principal regarding the selection of some or all of the assumptions to be used in the actuarial services. In doing so, the actuary should be guided by paragraphs 2.6 – 2.9 of ISAP 1, taking into account IAS 19's requirements regarding assumptions used to measure defined benefit post-employment plans, termination benefits, or other long-term benefits. IAS 19 requires that these assumptions be unbiased and mutually compatible, and that financial assumptions be based on market expectations at the measurement date for the period over which the obligations are to be settled.

Comment [Z7]: See comment in 2.5.

Comment [Z8]: The Standard does not cover the general practice when the valuation is prepared before the measurement date and preliminary results are assessed on the measurement date based on materiality; therefore assumptions are set in advance. The current wording actually excludes this approach.

The Standard should disclose that assumptions are possible to be set at an earlier date than the measurement date as long as the impact is assessed as of the measurement date and necessary revaluations are performed based on materiality.

2.6.1 General Approach for Selecting Assumptions – When advising the principal on the selection of actuarial assumptions, the actuary should:

a. Identify the types of assumptions needed to perform the actuarial services;

b. Evaluate information relevant to each type of assumption;

i. With respect to financial assumptions, the actuary should review information on market expectations at the measurement date. Such data may include corporate and government bond yield curves, yields on nominal and inflation-indexed debt, recent changes in price indices, forecasts of inflation, employment data and projections, and economic data and analyses prepared by experts.

ii. With respect to demographic assumptions, the actuary should review information that, in the actuary's professional judgment, is relevant to the population covered by the reporting entity's employee benefits. Such data may include: the experience of the covered population to the extent credible; analyses prepared by experts such as published tables or experience studies; studies or reports on general trends relevant to the particular demographic assumption; the reporting entity's future expectations; and relevant factors known to the actuary that may affect future experience such as the economic conditions of the geographic area or industry, availability of alternative employment, and the reporting entity's human resource policies or practices.

c. Consider which parameters assumptions should vary by taking into account the degree to which a particular parameter (for example, gender, age, birth year, service, employment type, or calendar year) is expected to affect future plan experience with respect to that assumption, and whether different assumption formats are appropriate for different segments of the covered population;

d. Recommend assumptions that are in accordance with IAS 19 (that is, they are unbiased, mutually compatible and, in the actuary's opinion, would be appropriate to represent the reporting entity's best estimate).

2.6.2 Mortality Assumption – When advising the principal on the selection of the mortality assumption, the actuary should recommend a mortality assumption that reflects the mortality of plan members both during and after employment taking into consideration expected changes in members' future mortality rates. The actuary may do so by using a generational table (that is, a matrix including separate mortality tables for each year of birth). The actuary may also use simplified mortality projection methods such as projecting the mortality rates for an appropriate period.

2.6.3 Discount Rate Assumption – When advising the principal on the selection of the discount rate assumption, the actuary should recommend an assumption that takes into account IAS 19's requirement that the discount rate reflect market yields at the measurement date on high quality corporate bonds or government bonds, as appropriate, where such bonds should be consistent with the currency and estimated term of the employee benefit obligation.

a. General Approach – Unless the actuary has determined that a simplified approach is appropriate (as described in c. below), the actuary should:

i. Project cash flows on and after the measurement date of benefits attributed to employee service up to the measurement date;

ii. Identify an appropriate spot-rate yield curve (as described in b. below);

iii. Use the spot rates to determine the present value of the defined benefit obligation at the measurement date; and

iv. Determine a single weighted-average discount rate that produces substantially the same present value of the defined benefit obligation for disclosures in the IFRS report and other appropriate calculations (for example, net interest or service cost).

b. Appropriate Yield Curve – The actuary may develop an appropriate yield curve from bond yield data at the measurement date. Alternatively, the actuary may apply a third party's yield curve, which the actuary has determined is appropriate for the purpose of selecting an IAS 19 discount rate (or has adjusted so as to make it appropriate).

i. Corporate Bond Characteristics – When developing a yield curve – or assessing the appropriateness of (or making adjustments to) a third party's yield curve – from a bond universe that includes corporate bonds, the actuary should consider the characteristics of those bonds, including the following:

- Currency – Corporate bonds should be denominated in the same currency as the employee benefits are denominated.

Comment [Z9]: We suggest to complete the paragraph with the following sentence: "The actuary should consult with from the principal whether and how effects of legislative changes should be taken into account, if applicable."

Comment [Z10]: This is true only for post-employment benefit plans and is not necessarily true for e.g. other long term benefits.

More accurate wording would be "during and if the employee benefit plan requires after employment" or similar.

Comment [Z11]: The Standard does not give guidance how to deal with country risk in high interest rate environment. Preserving prudence and avoiding volatility of the obligation might be a challenge under such circumstances. However possibly this is a deficiency of the IAS rather than the ISAP.

Comment [Z12]: IAS19R uses the projected unit credit method. Why does IASP3 does not use this term at all? Consistency with IAS would be welcome when referring to specific methods.

Comment [Z13]: IASB currently have a project on determining the discount rate for IAS19R. If anything is published by the time ISAP3 is finalized, it should be taken into consideration.

Comment [Z14]: We recommend using numbering instead of bulleting, it makes easier the references.

- Quality – Corporate bonds should be of high quality. In using bond-quality data from internationally recognised credit rating agencies, the actuary should be aware of rating differences between such agencies and have (or understand the yield curve developer's) rules for dealing with such differences. The actuary should also be aware of time lags in the credit rating process. Under normal market conditions, time lags may be insignificant. Under abnormal conditions, the actuary may need to adjust the yield curve for time lags.
- Type – The cash flows of some corporate bonds are not fully predefined in timing and amount (for example, convertible or callable bonds). If such bonds are included, the actuary should understand the effect on the yield curve and make adjustments as appropriate.
- Market Depth – High quality corporate bonds should be included only if the market for such bonds is deep overall; however, the market need not be deep at every duration. A market is considered by the Bank for International Settlements, for example, to be deep and liquid when "participants can rapidly execute large-volume transactions with little impact on prices."[2]. Indicators of market depth include trading volume and bid-ask spreads (for example, wide bid-ask spreads may indicate a lack of depth).
- Outliers – Market yields on some high quality corporate bonds may be substantially different from the yields on most bonds of similar quality and duration included in the universe. The actuary should have (or understand the yield curve developer's) rules for dealing with such outliers. For example, the actuary (or yield curve developer) might exclude such bonds from the universe, or the actuary may make appropriate adjustments to account for a third party's inclusion of outliers in developing the yield curve.

Comment [Z15]: The definition of „deep and liquid market" would have a better place in the Glossary.

ii. Curve-fitting, Interpolation, and Extrapolation – When the actuary is constructing the yield curve from the available bond data, the actuary should apply appropriate curve-fitting, interpolation, or extrapolation techniques. The actuary may use interpolation or extrapolation techniques to estimate yields at durations where the actuary considers the appropriate bond market data unreliable or such data does not exist. Such techniques may take into account (with an appropriate spread adjustment) other market data sources such as yields on government or lower-rated corporate bonds or the swaps market. For example, at durations beyond the longest dated market bond, the actuary may use extrapolation techniques built off spot rates or forward rates, or price consistent approaches. The actuary should be mindful that the choice of extrapolation technique may have a significant impact on the measurement of the liabilities when projected benefit cash flows extend beyond the longest dated market bond. In particular, relatively small

[2] Committee on the Global Financial System, Publication No. 13, October 1999.

changes in the shape of the yield curve at shorter durations may be magnified when extrapolated over a long period. Similarly, when the actuary is using a third party's yield curve, the actuary should understand how that third party has constructed its yield curve.

c. Simplified Approach – The actuary may use a simplified approach to recommend a discount rate rather than following the general approach described in a. above. The actuary should understand the data and assumptions on which the simplified approach is based and the circumstances in which it can be applied appropriately. The simplified approach should take into account both the duration of the projected benefit cash flows and their shape (that is, whether the cash flows over time are smooth or lumpy).

   i. The actuary may recommend a single discount rate that, in the actuary's professional judgment, approximates the weighted-average rate that would be determined under a.iv. above.

   ii. The actuary may apply a market index or other reference rate, with adjustments if appropriate. The actuary should understand the bond data and methodology used to construct the index or reference rate, and adjust the rate as appropriate for the duration and shape of the projected benefit cash flows.

2.6.4 General Price Inflation Assumption – When the actuary is advising the principal on the selection of a general price inflation assumption, the actuary should review information on market expectations at the measurement date. Such information may include: changes in price indices, implicit price deflators, yields on nominal and inflation-indexed debt (taking into account the effect of any significant supply-demand imbalances), forecasts of inflation, relevant regional factors, and central bank monetary policy.

2.6.5 Assumptions Regarding Changes in Employee Benefit Levels – Depending on the nature of the employee benefits, future benefit levels may reflect factors other than general price inflation. When the actuary is advising the principal on the selection of an assumption about future benefit levels, the actuary should consider relevant factors such as merit or promotional salary increases, investment returns on actual or notional assets, technological advances, changes in benefit utilisation or delivery patterns, changes in social insurance benefits, changes in offsets of benefits provided by other parties, expected changes in mandated benefits, and changes in the demographic profile of plan participants.

2.6.6 Assumptions Selected for Other Purposes – When advising the principal on the selection of assumptions, the actuary may consider assumptions selected for other purposes (such as to determine funding of the employee benefit plan) or demographic assumptions used at a prior measurement date, if in the actuary's professional judgment, those assumptions satisfy IAS 19's requirements.

2.6.7 Using Prescribed Assumptions – When using assumptions prescribed by the principal, the actuary should be guided by paragraph 2.8 of ISAP 1. If, in the actuary's professional judgment, assumptions prescribed by the principal fail in a material manner to conform to IAS 19, other relevant IFRSs or the reporting entity's accounting policies, the actuary should be guided by paragraph 2.3.

2.6.8 Change in Process for Developing Assumptions – The actuary generally should apply a consistent process from year to year to develop recommended assumptions

for a particular reporting entity. When the actuary considers it appropriate to change the process used to develop a recommended assumption, the actuary should discuss the change with the principal, and should seek guidance from the principal regarding what, if any, information about the change should be disclosed in the report. For example, if the principal determines that the change in the assumption-setting process may be subject to IAS 8, the principal may ask the actuary to disclose the nature of the change and its general effect in the report.

2.7 **Plan Assets** – Plan assets often play a significant role in the management of an employee benefit plan. When the actuarial services take plan assets into account, the actuary should be guided by the following:

2.7.1 Asset Values Supplied by Others – The actuary may rely on asset values prepared by a third party (such as a trustee or investment manager) and, when doing so, should be guided by paragraph 2.3.3 of ISAP 1.

2.7.2 Qualifying Insurance Policies – When plan assets include qualifying insurance policies, the actuary should appropriately reflect those policies in the calculation of the obligation. For example, the actuary should appropriately differentiate between the reporting entity's employee benefit obligations and those that an insurer has assumed.

2.7.3 Asset-related Benefit Liabilities – The actuary should apply professional judgment to appropriately value employee benefits when the benefit level is affected by the value of plan assets (for example, when benefit levels are linked to the return on plan assets (see paragraph 2.6.5) or depend on whether there is a surplus).

2.7.4 Asset Ceiling – When there is a surplus (that is, the fair value of plan assets exceeds the present value of the defined benefit obligation for the plan), the actuary should consider whether the asset ceiling applies. The asset ceiling applies when the surplus exceeds the present value of economic benefits available to the reporting entity in the form of refunds from the plan or reductions in future contributions to the plan. If the asset ceiling applies – or the actuary is uncertain whether it applies – the actuary should seek guidance from the principal whether to apply International Financial Reporting Interpretations Committee Interpretation number 14 (IFRIC 14).

2.8 **Attribution of Benefits to Service Periods** – When advising the principal on the attribution of plan benefits to service periods, the actuary should exercise professional judgment to address plan designs whose treatment is not clear from IAS 19, such as how to attribute benefits if a benefit formula is expressed as a constant proportion of current salary.

2.9 **Proportionality** –The effort involved in measuring employee benefit obligations should be proportional to the level of accuracy established for the assignment, taking into account materiality. The actuary is not required to recommend a particular type of assumption or a more refined approach when, in the actuary's professional judgment, its use is not expected to produce materially different results. For example, using a simplified approach to set the discount rate or assuming that all participants elect the most common option when a pension plan offers several actuarially equivalent life annuity payment options, may not produce IAS 19 results that are materially different from a more refined approach. In this paragraph, all references to materiality are with respect to the actuarial services (see paragraph 2.2.1).

Comment [Z16]: Besides proposing assumptions as of one particular measurement date the role of the actuary is crucial in back-testing previously applied assumptions as usually other related parties do not have the professional insights to fully understand the development of the obligation and how it indicates the appropriateness of the assumptions themselves and the assumption setting processes.

The Standard should emphasize more that the actuary is expected to draw conclusions about the quality of the assumptions and the assumption setting processes based on experience analyses.

Comment [Z17]: See previous comment on "seek guidance".

Comment [Z18]: See previous comment on "seek guidance".

Section 3. Communication

3.1 **Disclosures in the Report** – In addition to complying with Section 3 of ISAP 1, the actuary should disclose in the report:

a. Any material deviation from the guidance in this ISAP, where materiality is with respect to the actuarial services (see paragraph 2.2.1) (1.3.3);

b. Any unresolved material errors, omissions, or non-conformance with IAS 19, other relevant IFRSs, or the reporting entity's accounting policies (2.3);

c. Any reliance on the principal's representations regarding constructive obligations (2.4); and

d. Any information regarding a change in the process for selecting assumptions that is requested to be disclosed (2.6.8).

Comment [Z19]: See previous comment on compliance with IAS 19R reporting requirements.

APPENDIX

Note: this appendix is provided for informational purposes, and is not part of the ISAP.

Background

IAS 19 prescribes employers' accounting and disclosure requirements for their employee benefits other than share-based payments, which are accounted for in accordance with IFRS 2 Share-based Payment. On 16 June 2011, the IASB published an amended IAS 19. That amended standard is applicable for annual accounting periods beginning on or after 1 January 2013, with early adoption permitted.

A key principle of IAS 19 is that it generally requires the cost of providing employee benefits to be recognised in the period in which the employee performs services, rather than when the benefit is paid.

Comment [Z20]: Whilst issuing ISAP3 is a big step it would be great to have the relevant ISAPs issued by the time the relating IAS is effective. This is more a comment for Insurance phase2.

Comment [Z21]: We recommend placing this short introduction of IAS 19 to the Introduction.

Categorization of Employee Benefit Plans

IAS 19 defines four categories of employee benefits (excluding equity share-based compensation):

- **Short term benefits** expected to be settled wholly before twelve months after the end of the annual reporting period in which the employees render the related services, such as wages, salaries and social security contributions, paid annual leave and paid sick leave, profit-sharing and bonuses and non-monetary benefits (such as medical care, housing, cars and free or subsidised goods or services) for current employees.
- **Post-employment benefits**, such as defined contribution retirement plans, pensions, lump sum payments on retirement, post-employment life insurance and post-employment medical care. This category is further broken down between defined benefit and defined contribution plans:
  - Under a defined contribution plan, the reporting entity pays fixed contributions into a fund but has no legal or constructive obligation to make further payments if the fund does not have sufficient assets to pay all of the employees' entitlements to post-employment benefits;
  - A defined benefit plan is a post-employment benefit plan other than a defined contribution plan.
- **Other long-term employee benefits**, such as long-service leave or sabbatical leave, jubilee or other long-service benefits, and long-term disability benefits.
- **Terminations benefits** payable as a result of the reporting entity's decision to terminate the employee or the employee's decision to accept an offer of benefits in exchange for termination of employment.

Accounting Treatment Depends on Categorization

Short-term benefits and defined contribution post-employment benefits. For short-term benefits or defined contribution post-employment plans, the undiscounted amount of the benefits or contributions expected to be paid is recognised in the accounting period the employee renders service.

Defined benefit post-employment plans and other long-term employee benefits. Defined benefit post-employment benefits and other long-term employee benefits are generally attributed to employees' service. The employer recognises a balance sheet liability/asset equal to the present value of these benefits, attributed to service through the measurement date (the "present value of the defined benefit obligation"), minus the fair value of plan assets at the measurement date. This net liability/asset is called the net defined benefit liability/asset. The net asset recognised on the

employer's balance sheet is limited to the "asset ceiling," defined as the present value of economic benefits available to the employer as refunds from the plan and/or as reductions in future contributions.

Employers must recognise service cost and net interest (on the net defined benefit liability/asset) in the income statement. Service cost includes the cost of benefits attributed to service during the accounting period, changes in the defined benefit obligation due to plan amendments or curtailments occurring in the accounting period, and gains or losses from settlements occurring in the accounting period. Net interest is calculated by applying the discount rate (used to measure the defined benefit obligation) to the net defined benefit liability/asset, adjusted for contributions and benefit payments during the accounting period.

All other changes in the net defined benefit obligation/asset, including the difference between actual investment return and the expected return determined using the discount rate, changes in the defined benefit obligation from discount rate or other assumption changes, and experience gains and losses, are recognised immediately in Other Comprehensive Income (OCI).

IAS 19 provides a special rule for long-term disability or employment-related injury benefits. When the level of benefit is the same for any employee regardless of years of service, the expected cost of those benefits is recognised when an event occurs that causes a long-term disability or employment-related injury.

Termination benefits. Termination benefits are triggered by the termination of employment, and are recognised when the reporting entity can no longer withdraw the offer of those benefits or, if earlier, when the reporting entity recognises associated restructuring costs. Termination benefits may take various forms, such as lump sum payments, pension benefit enhancements, or salary continuation for a specified period.

IFRS Report Disclosures

IAS 19 requires the reporting entity to disclose information in its IFRS report that:

- Explains the characteristics of defined benefit plans and risks associated with them;
- Identifies and explains the amounts in the IFRS report arising from defined benefit plans; and
- Describes how its defined benefit plans may affect the amount, timing, and uncertainty of the reporting entity's future cash flows.

Actuarial engagements in connection with IAS 19 often include assisting reporting entities in meeting these disclosure objectives. Areas where actuaries may provide particularly valuable input include:

Comment [Z22]: We recommend completing the paragraph with the sentence of "A common understanding is needed between the actuary and the principal regarding the areas and depth the actuary provides input for the disclosures."

- Disclosures about plan characteristics or risks that are unusual, reporting entity-specific or plan-specific, such as post-employment medical benefit plans with no lifetime claims limit, plan-specific limitations on refunds of surplus to the employer, concentrations of plan assets in one class of investments, or counter-party risk associated with material expected insurance recoveries;
- Disclosures about existing risk management strategies such as enterprise risk management, asset-liability matching, or longevity swaps;
- Explanation of amounts in the IFRS report, including the reconciliation of amounts shown in the IFRS report from the beginning to the end of the year;
- The appropriate level of aggregation or disaggregation of employee benefit plans according to their characteristics and risks;

- Disclosures about how defined benefit plans may affect the amount, timing, and uncertainty of the reporting entity's future cash flows (such as expected funding contributions);
- Disclosures about the maturity profile of the defined benefit obligation; and
- Disclosures about the significant assumptions used to determine the present value of the defined benefit obligation, their "reasonably possible" variation, and the consequent change in the present value of the defined benefit obligation at the measurement date. IAS 19 does not establish a numeric threshold for determining significance or reasonably possible variations, but refers to IFRS 7 (paragraph B19) for the principles to be used to quantify "reasonably possible" variations.