

## Memorandum

**To:** All Fellows, Affiliates, Associates and Correspondents of the Canadian Institute of Actuaries and Other Interested Parties

**From:** Charles C. McLeod, Chairperson  
Actuarial Standards Board  
Nicholas Bauer, Chairperson  
Designated Group

**Date:** November 30, 2009

**Subject:** **Final Standards of Practice – Part 1000 General and Part 2000 Insurance, to conform to the adoption of International Financial Reporting Standards (IFRS) as Canadian GAAP**

*Document 209114*

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### INTRODUCTION

The attached final Standard of Practice was approved by the Actuarial Standards Board (ASB) on November 24, 2009.

A notice of intent on this matter was published on December 31, 2008, with a comment period ending on March 15, 2009 (<http://www.actuaries.ca/members/publications/2008/208093e.pdf>). An exposure draft was published on July 15, 2009 with a comment period ending on September 18, 2009 (<http://www.actuaries.ca/members/publications/2009/209071e.pdf>).

Changes compared to the exposure draft are available in a red-lined version. In the opinion of the ASB these changes are minor and do not require re-exposure pursuant to the ASB's Policy on Due Process for the Adoption of Standards of Practice.

### BACKGROUND

As explained in the notice of intent as well as in the cover memo to the exposure draft, the Canadian Accounting Standards Board has announced that International Financial Reporting Standards (IFRS) will become Generally Accepted Accounting Principles (GAAP) in Canada for Publicly Accountable Enterprises (PAEs) as of January 1, 2011, by importing into Canadian GAAP the entirety of IFRS without modification. Reference to GAAP will thence be the same as reference to IFRS for PAEs. To avoid confusion, references to IFRS mean references to Canadian GAAP as it will exist from January 1, 2011.

The Office of the Superintendent of Financial Institutions (OSFI) and the Autorité des marchés financiers (AMF) have confirmed that all insurance companies under their jurisdictions will be considered PAEs and will, thus, have to convert to IFRS, and we expect that other jurisdictions will follow suit.

A key difference between current Canadian GAAP and IFRS is that the former is entity-specific while the latter is contract-specific, meaning that what will govern accounting for, and valuation of, contracts is the nature of the contracts and not the type of institution issuing them.

A significant outcome of the change to IFRS is that accounting for, and valuation of, contracts typically issued by insurers will be governed by different parts of IFRS.

Insurance contracts, as defined in IFRS 4, will be valued under IFRS 4, which specifies that on conversion to IFRS, the insurer's current accounting policy should continue to be used. This means that insurance contracts will continue to be valued in conformity with current Canadian actuarial Standards of Practice, amended as set out in the attached final Standard of Practice.

Financial instruments other than insurance contracts will be valued as set out in International Accounting Standard (IAS) 39.

Service contracts will be valued as set out in IAS 18.

IFRS 4 specifies that a reinsurance contract is an insurance contract. Consequently, IFRS 4 applies equally to insurance and reinsurance contracts. IFRS 4 stipulates that reinsurance assets may not be offset against insurance liabilities (i.e., "netting" is not permitted).

The current Standards of Practice of the Canadian Institute of Actuaries (CIA) are inconsistent with IFRS. The purpose of this final Standard of Practice is to remove those inconsistencies.

The ASB is not proposing to introduce practice-specific Standards of Practice with respect to the valuation of contracts outside the scope of IFRS 4. The reason is that IFRS already contain guidance with respect to the classification of contracts and the valuation of financial instruments and service contracts. Specifically, the ASB is not proposing to introduce Standards of Practice for the valuation of service contracts, nor for the valuation of financial instruments other than insurance contracts. The valuation of those types of contracts will be governed by IAS 18 Revenue and IAS 39 Financial Instruments, as well as the General Standards of Practice.

That does not mean, however, that members will lack guidance. The ASB notes that the Practice Council of the CIA has published guidance with respect to both the classification of contracts and the valuation of financial instruments and service contracts, based on the International Actuarial Standards of Practice published by the International Actuarial Association.

Finally, IFRS 4 requires, permits or prohibits – depending on the circumstances – the separation of deposit components within insurance contracts, and requires, under certain circumstances, the unbundling of derivatives embedded in insurance contracts, unless those derivatives are themselves insurance contracts. The ASB does not propose to introduce Standards of Practice with respect to these matters either, but again, the

guidance published by the CIA also incorporates assistance to members with respect to them.

### **DESIRED OUTCOME**

The desired outcome is to achieve conformity and consistency with IFRS, and the changes are aimed at achieving that objective, as of January 1, 2011, which is the announced implementation date of IFRS as Canadian GAAP. The ASB is aware that IFRS 4 is destined to be revised, that the International Accounting Standards Board (IASB) has published a discussion draft to that end, and that it continues to study the matter. The target date of the IASB for the publication of an exposure draft is the end of 2009. None of the changes anticipate that revision. They are based on the current version of IFRS 4, since the revision is not expected to become effective before 2013.

The definition of certain terms under IFRS differs from previous common usage in Canada and the terminology of the current Standards of Practice. To ensure consistency, the IFRS 4 definitions of certain terms, such as “insurance contract” and “policyholder”, have been incorporated into the Definitions in subsection 1110 of the General Standards of Practice, which in turn has necessitated follow-on changes in terminology (see “Other Issues” below).

### **COMMENTS RECEIVED**

Comments on the exposure draft were received from two CIA members and the CIA Practice Council. All the comments were reviewed and considered prior to the preparation of the final Standard of Practice. A summary of these comments and the responses from the Designated Group follow, except that comments concerning formatting or placement of words and phrases are omitted.

#### **Scope of the Standards of Practice**

##### *Comments received*

The Practice Council thought that due to the introduction of the definition of “insurer” (per 1110.28), and the use of that term at times in what seemed to be its current sense (i.e., an insurance company), it was not clear whether the Standards of Practice apply only to the actuaries of regulated entities or to all actuaries who value the liabilities of an insurer, under the new definition of that term.

##### *Treatment in the Final Standard of Practice*

In order to ensure that there is no possibility of confusion, the following modifications were made:

The third example under “Extension of Scope” in the General Standards of Practice, set out in paragraph 1230.11, has been revised to show that some parts of the Insurance Standards apply to all actuaries who value insurance contract liabilities for GAAP purposes, while other parts apply only to appointed actuaries (as defined) who have the necessary authority and legal immunity. The sections, the applications of which are restricted to appointed actuaries, are 2400 and 2500, and their Scopes (paragraphs 2420.01 and 2510.01, respectively) explicitly say so. Nonetheless, to further ensure that the point is evident, all of the references to

“actuary” in the italicized portions of sections 2400 and 2500 have been changed to “appointed actuary”.

The text of paragraph 2120.03 has been modified to further clarify that part 2000 applies to the work of all actuaries who value insurance contract liabilities for purposes of inclusion in general purpose financial statements prepared in accordance with GAAP (whether applicable GAAP is IFRS or not). As explained above, sections 2400 and 2500 are excluded from that general application and only apply to appointed actuaries.

### **Valuation of Reinsurance Recoverables**

#### *Comments received*

The Practice Council’s preference was that the opinion of the actuary should remain as it is currently, that is, cover only the net liabilities and not be extended to cover each of the gross policy liabilities and reinsurance recoverables.

#### *Treatment in the Final Standard of Practice*

While the ASB concurred with the primary importance of the net insurance contract liabilities, it disagreed with the view that the actuary should only take responsibility for, and opine on, the net insurance contract liabilities – a figure that does not appear on the IFRS balance sheet – and not opine on the insurance contract liabilities and reinsurance recoverables that do so appear. The ASB agreed, however, that where GAAP other than IFRS applies, the actuary **may** opine on the net insurance contract liabilities (unless the terms of the engagement require otherwise).

### **Extension of Scope (subsection 2120)**

#### *Comments received*

The Practice Council thought that the proposed wording of paragraph 2120.04 obligated actuaries to value all policy liabilities [of PAEs] by the current method (e.g., Canadian Asset Liability Method (CALM) for life insurance) for any statutory or regulatory purpose other than the preparation of financial statements in accordance with GAAP, such as for Minimum Continuing Capital and Surplus Requirements (MCCSR) filing purposes.

#### *Treatment in Final Standard of Practice*

In order to ensure that there is no misinterpretation of the intention, the text of paragraph 2120.04 was modified to clarify that the scope is extended to cover all policy liabilities if, and only if, that is required by statute, regulation or regulatory guideline.

## **Other Issues**

### *Comments received*

The Practice Council felt that paragraph 1730.21 needed a reference to the health of insured life in order to be clear.

One member observed that “unamortized realized capital gains” will not exist under IFRS and should be removed from the Standards of Practice.

The Practice Council suggested that the reference to “deposit liabilities” in paragraph 2130.16 should be removed.

One member requested that the reference to accounting treatment in paragraph 2140.04 be removed, since this should not be governed by actuarial Standards of Practice.

The Practice Council suggested that the references to Single Premium Deferred Annuity (SPDA) and Administrative Services Only (ASO) contracts in paragraph 2320.27 be deleted, as they would not be considered insurance contracts under IFRS.

### *Treatment in Final Standard of Practice*

The ASB agreed with the above suggestions, and the Standard of Practice was modified accordingly.

## **PROCESS AND TIMETABLE**

The Actuarial Standards Board’s Policy on Due Process for the Adoption of Standards of Practice has been followed in the preparation of this final Standard of Practice.

The final Standard of Practice was adopted by the Actuarial Standards Board on November 24, 2009.

The effective date of the final Standard of Practice is January 1, 2011 but, in the case of financial statements prepared in accordance with IFRS, it only applies to work in respect of interim or annual statements prepared pursuant to IFRS, that is, relating to financial years beginning on or after January 1, 2011. Early implementation is prohibited.

CCM, NB