Canadian Institute of Actuaries
Institut canadien des actuaires

Draft Guidance

Disclosure of Actuarial Matters – Actuarial Comments

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DRAFT GUIDANCE

DISCLOSURE OF ACTUARIAL MATTERS – ACTUARIAL COMMENTS

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COMMITTEE ON THE ROLE OF APPOINTED/VALUATION ACTUARY

JANUARY 1996

Ce projet de conseils est disponible en français

Disclosure of Actuarial Matters – Actuarial Comments

As the "Disclosure of Actuarial Matters" note indicates, the accounting principle that follows, and the illustrative examples, have been largely a collaborative effort between the CIA and CICA. The CIA's input has come from the Committee on the Role of the Appointed/Valuation Actuary. In June of this year, that committee was formed by Council and asked to take a lead role in development of proposed disclosure of actuarial matters in financial statements. The committee's initial thoughts were circulated to members in September and discussed at the Seminar for the Appointed Actuary in Montréal. Several written comments from members were received. The material enclosed encompasses the committee's current thinking together with that of the CICA. It is being exposed as a draft for comment.

In interpreting the attached material, please read both the guideline and the two sets of illustrative examples. As well, the following recommendations from the committee might be helpful in applying the guidelines:

1. The disclosure is intended to help an interested reader of financial statements understand some of the intricacies of the balance sheet and income statement of a life insurance company. It is not intended to provide proprietary information to competing companies. Therefore, disclosure of items that might be viewed as proprietary, such as detailed valuation assumptions, is not recommended.

2. Ultimately, disclosure might advance to a level where a sophisticated analyst could gain insight into the company's operations. We expect disclosure, however, to be an evolutionary process as companies determine what competitors are doing and what readers want. As such initial disclosure might be broader and more educational leading towards more detailed analytic disclosure in coming years.

3. It is important the major risks to which a company is exposed be explained. Management actions to mitigate the risks should be discussed. Dynamic solvency testing (DST) results should not be disclosed because many scenarios are of low probability and could mislead readers as to their importance. However, DST results will be important in guiding actuaries as to critical risks that should be discussed.

4. Total provision for adverse deviations (PAD) should be disclosed. The attached draft guidance note indicates that such disclosure should be considered – our committee feels the disclosure should be required. Disclosure could take the form of an absolute dollar amount of PAD or a percentage of liability. Disclosure of PAD by assumption is not recommended. Disclosure of PAD by product line and/or territory may be appropriate.

5. Disclosure of sensitivity to interest rate changes is difficult for products subject to VTP 9 cash flow testing because the liability already provides for interest rate sensitivities. It is recommended that disclosure quantify at least the extent of reserve increase needed to absorb a 1% change in interest rates and maintain the same level of C-3 and other margins as is currently in the reserves.

6. Contrary to an earlier CIA draft recommendation, the impact of reinsurance on earnings need not be disclosed, however, the reserve impact should be disclosed.

7. The CICA accounting standard on financial instruments calls for determination – beginning in 1997 – of both fair value of assets and liabilities, where practical. The attached draft guidance note is consistent with that standard. The CIA committee believes that calculating fair value of liabilities will be expensive and difficult, with little added benefit. In general, assets and liabilities change value in tandem, where they don't, disclosure should be mandated. Where they do, disclosure of the fair value of surplus, together with a discussion of the interrelationship between asset and liability values, should be appropriate disclosure. Members are particularly

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invited to comment on this issue as we need to build a case to the CICA to provide an exception to its standard for life insurance enterprises.

8. Disclosure as proposed in the attached guideline must be made through notes to published financial statements. Any additional disclosure by companies, including the specific added disclosure below, could be in an MD&A if one exists. Note that if no published financial statement exists, disclosure should be made to the relevant regulator.

9. Only material items should be disclosed.

The CICA draft guideline deals with disclosure related to actuarial liabilities. In addition, the CIA feels disclosures related to capital adequacy and liquidity are important. A brief discussion of each area follows.

Capital Adequacy

Companies should disclose their MCCSR ratio – once the ratio is felt to be stable – but not later than 1997. For foreign branches, the appropriate capital adequacy standards, if other than MCCSR, should be disclosed. Disclosure should not include a separation of available and required elements because of the potential confusion created by available capital differing from balance sheet capital and surplus. An explanation of the change in ratios from one year to the next is also suggested. Where transition rules are material to the ratio, this impact should be disclosed.

Liquidity

The availability of liquid assets to meet cash demands is critical to any financial institution. Disclosure should be made of both assets readily available (both book and market values) and known and potential liquidity needs of liabilities. Any unique liquidity requirements in the near term (i.e., a large amount of GIC's maturities) should be discussed.

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