

**ABI STATEMENT OF
RECOMMENDED PRACTICE ON
ACCOUNTING FOR INSURANCE
BUSINESS (SORP)
DECEMBER 2005
(as amended in December 2006).**

STATEMENT BY THE ACCOUNTING STANDARDS BOARD

The aims of the Accounting Standards Board (the ASB) are to establish and improve standards of financial accounting and reporting, for the benefit of users, preparers, and auditors of financial information. To this end, the ASB issues accounting standards that are primarily applicable to general purpose company financial statements. In particular industries or sectors, further guidance may be required in order to implement accounting standards effectively. This guidance is issued, in the form of Statements of Recommended Practice (SORPs), by bodies recognised for the purpose by the ASB.

The Association of British Insurers (ABI) has confirmed that it shares the ASB's aims of advancing and maintaining standards of financial reporting in the public interest and has been recognised by the ASB for the purpose of issuing SORPs. As a condition of recognition, the ABI has agreed to follow the ASB's code of practice for bodies recognised for issuing SORPs.

The code of practice sets out procedures to be followed in the development of SORPs. These procedures do not include a comprehensive review of the proposed SORP by the ASB, but a review of limited scope is performed.

On the basis of its review, the ASB has concluded that the SORP has been developed in accordance with the ASB's code of practice.

The ASB's review also considers whether the SORP appears to contain any fundamental points of principle that are unacceptable in the context of present accounting practice or to conflict with an accounting standard or the ASB's plans for future standards. Because the SORP reflects an interplay between general accounting practice, the requirements of Schedule 9A of the Companies Act 1985 and detailed regulatory requirements (the FSA Rules) there are aspects of insurance accounting that do not align with other accounting practice. These include: the deferral of acquisition costs as assets; the inclusion of both equity and liabilities in the Fund for Future Appropriations; the measurement of provisions for liabilities to policyholders on a regulatory, solvency basis rather than at the best estimate of the expenditure required to settle them; and the measurement of such liabilities using discount rates based on asset yields, which is consistent with the FSA Rules but is inconsistent with guidance in FRS 12 'Provisions, Contingent Liabilities and Contingent Assets', FRS 17 'Retirement Benefits' and FRS 19 'Deferred Tax'.

December 2005

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PART 1 - Preface

- Introduction
- 1 The recommendations in this Statement only apply directly to insurance companies and groups that are subject to the requirements of Schedule 9A to the Companies Act 1985 (“the CA 85”) and UK generally accepted accounting principles (UK GAAP). The Statement does not address alternative methods of accounting for shareholders’ profits from long term insurance business such as the European Embedded Values Principles, which have been developed by the CFO Forum.
 - 2 This SORP has no direct application to entities that are required or choose to adopt international accounting standards (IAS) as the basis for financial reporting. These entities however are encouraged to have regard to its provisions insofar as this is compatible with the requirements of IAS.
 - 3 The recommendations in this statement are made in the context of the deferral and matching accounting methodology and the modified statutory solvency basis for life business and within the constraints imposed by Schedule 9A to the Companies Act 1985 (“the CA85”). Within those limitations, they should be regarded as laying down best practice on accounting for insurance business in the United Kingdom.
 - 4 The EU Commission has issued a Regulation requiring all listed entities within its jurisdiction to prepare their consolidated accounts for accounting periods beginning on or after 1 January 2005 in accordance with IFRS to the extent that they have been endorsed by the Commission. In the United Kingdom, listed parent companies in their own financial statements, and unlisted companies and groups, have the option to adopt IFRS from that date. The International Accounting Standards Board (IASB) has published an international financial reporting standard (IFRS 4) on insurance contracts as phase I of a longer term project on accounting for insurance contracts.
 - 5 FRS 26 (Financial Instruments: Measurement) applies to those entities preparing accounts under UK GAAP that are either listed or prepare their financial statements in accordance with the fair value accounting rules in the CA 85*. Under this standard, an entity must not account for financial instruments as an insurance contract unless they are rights and obligations under an “insurance contract” as defined in Appendix C of FRS 26, which is taken from IFRS 4, or contain a discretionary participation feature as defined in that Appendix. In particular, FRS 26 will apply to unlisted insurers that hold derivative instruments measured at fair value as this treatment is now governed by the fair value accounting rules.
 - 6 FRS 26 requires contracts previously accounted for as insurance but which do not meet the conditions set out above, to be accounted for as investment contracts.
 - 7 FRS 26 is effective for listed entities with effect from accounting periods beginning on or after 1 January 2005 and for unlisted entities adopting the fair value accounting rules in the CA 85 for accounting periods beginning on or after 1 January 2006, although voluntary

* The ASB is considering proposals to extend the scope of FRS 26 with effect from accounting periods beginning on or after 1 January 2007 to all financial statements that are intended to give a true and fair view of a reporting entity’s financial position and profit or loss except those applying the FRSSSE.

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		compliance is permitted for accounting periods beginning on or after 1 January 2005 but not earlier.
	8	With effect from accounting periods ending on or after 23 December 2005, reporting entities that include a business which is a life assurance business (including reinsurance business) are required to comply with FRS 27 (Life Assurance) but early adoption of all or part of this standard is permitted. FRS 27 amends some of the provisions of this SORP and in addition imposes further disclosure requirements (see paragraphs 18 .)
Objectives	9	The principal objectives of this Statement are: (i) to set out recommended accounting practice for UK insurance entities within the framework of the CA 85 (and equivalent Northern Ireland legislation) in order to narrow the range of accounting practices and thereby enhance the usefulness of published accounting information; and (ii) to provide guidance on certain provisions of the CA85 and ASB Financial Reporting Standards relating to the financial statements of insurance undertakings where the Wording of these provisions requires clarification, or is insufficient in it to ensure a uniform interpretation of the requirements, or would result in an inappropriate diversity of accounting practices. (iii) In particular to provide guidance on: <ul style="list-style-type: none">○ Some aspects of the accounting for contracts issued by insurance undertakings which are subject to FRS 26 and do not satisfy the definition of an “insurance contract” or contain a “discretionary participation feature” as those terms are defined in FRS 26; and○ The implementation of certain aspects of FRS 27 (“Life Assurance”).
Reporting Framework	10	This Statement should be read in conjunction with the requirements of the CA85 applicable to insurance undertakings and, in particular, with Schedule 9A to the CA85.
	11	Financial Reporting Standards (FRSs) issued by, and Statements of Standard Accounting Practice (SSAPs) adopted by, the Accounting Standards Board (ASB) together with “Abstracts” of the Urgent Issues Task Force of the ASB (UITF) are applicable to all financial statements which are intended to give a true and fair view of an undertaking’s financial performance during an accounting period and of its financial position at the end of the period. Accordingly, all insurance undertakings to which this Statement applies are expected to follow these unless in special circumstances the requirement to give a true and fair view requires a departure from accounting standards. In such circumstances, the requirements of the accounting standard should be departed from only to the extent necessary to give a true and fair view and explanatory disclosures given in accordance with FRS 18 (Accounting Policies).
	12	The SORP takes into account all relevant UK accounting standards and other pronouncements that were extant at 31 March 2005. The references to FSA rules are to those rules applicable at 31 October 2005.

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General Insurance
Business
Accounting

- 13 This Statement generally requires the annual basis of accounting to be used for general insurance business. Under this method, the underwriting result disclosed in the financial statements comprises the result for the current accounting period and any adjustments during the current accounting period to estimates made in prior accounting periods.

Long Term
Insurance
Business
Accounting

- 14 UK insurance companies are regulated by the Financial Services Authority (the FSA) through the granting by the FSA of permission to carry on the regulated activities of effecting and carrying out contracts of insurance. The regulations made by the FSA, pursuant to the Financial Services and Markets Act 2000, are contained in the FSA Handbook of Rules and Guidance (the FSA Handbook). Under the FSA Principles for Businesses as amplified by FSA rules, insurance companies carrying on long term insurance business must:
- Maintain its long term insurance fund(s) separately;
 - keep adequate records to enable assets and liabilities attributable to the fund or funds to be identified;
 - use the assets of the fund only for the purposes of that business; and
 - make transfers out of the fund, other than reimbursements, only out of surplus ascertained after carrying out an actuarial investigation.
- 15 There is no requirement for financial statements prepared under the CA85 to be on the basis required for regulatory returns by the FSA rules. In consequence, CA85 accounts exhibit a number of differences in both form and content from the regulatory returns. In practice, however, before the implementation in the United Kingdom of the EU Insurance Accounts Directive, the transfer to shareholders from the long term business fund as determined in accordance with the FSA rules was also taken as the after tax result in the CA85 financial statements. This method of financial reporting came to be known as the “statutory solvency basis”.
- 16 For the purpose of preparing financial statements in accordance with Schedule 9A to the CA85 for contracts issued by insurance undertakings other than contracts which are required to be accounted for as investment contracts under FRS 26, two significant adjustments need to be made to the statutory solvency basis:
- (a) Firstly, to defer new business acquisition costs incurred where the benefit of such costs will be obtained in subsequent accounting periods; and
 - (b) Secondly, to consider the treatment of investment reserves, or reserves in respect of general contingencies or the specific contingency that the fund will be closed to new business, where such items are held within the long term business fund. These amounts, to the extent that they should be regarded as reserves rather than provisions, should be included as appropriate within shareholders’ capital and reserves or the fund for future appropriations.
- 17 The basis described in paragraph 16 is referred to as the “modified statutory solvency basis” (MSSB).

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- 18 FRS 27 (Life Assurance) forms part of UK GAAP with effect from accounting periods ending on or after 23 December 2005. The main provisions of this standard are summarised below:
- Policyholder liabilities for with-profits life assurance business subject to the FSA realistic capital regime to be measured at their realistic value with no deferral of acquisition costs;
 - Adjustments from the MSSB to meet the above requirements to be included in the profit and loss account with a transfer to or from the fund for future appropriations of the net amount of such adjustments;
 - Except where it arises from non-participating business written in a with-profits fund and is taken into account in the determination of the realistic liabilities of that fund, or is an amount recognised as an intangible asset as part of the allocation of fair values under acquisition accounting in accordance with FRS 7 “Fair values in acquisition accounting” which are subject to the measurement requirements under that standard, the value of in-force life assurance business can only be recognised as an asset if it is an entity’s existing accounting policy to recognise it as an asset (or deduction from a liability) and it excludes any value attributable to future investment margins;
 - Certain disclosures are required in relation to policyholders’ options and guarantees; and
 - A capital statement to be presented with associated disclosures.
- Interpretation 19 Paragraphs **82 to 312** should be read in the context of the Objectives as set out in paragraph **9** and the definitions set out in paragraphs **20 to 81**.

PART 2 - Definitions

The following definitions apply in this Statement.

Acquisition Costs	20	Schedule 9A to the CA85 defines acquisition costs as costs arising from the conclusion of insurance contracts including direct costs such as acquisition, commission or the cost of drawing up the insurance document or including the insurance contract in the portfolio, and indirect costs such as advertising costs or the administrative expenses connected with the processing of proposals and the issuing of policies. Policy renewal commission in the case of long term insurance business should be included under administrative expenses.
Administrative Expenses	21	Schedule 9A to the CA85 defines administrative expenses as costs of an administrative nature including those arising from premium collection, portfolio administration, handling of bonuses and rebates, and inward and outward reinsurance, including in particular staff costs and depreciation provisions in respect of office furniture and equipment insofar as these need not be shown under acquisition costs, claims incurred or investment charges.
Amortised Cost	22	The purchase price of a redeemable debt security or other fixed income security adjusted by any increase or decrease in value representing the proportion of any difference between the purchase price and the final redemption proceeds of the investment having regard to the period for which the investment has been held and the period remaining until the redemption date, or the assumed redemption date where a range of such dates exists.
Annual Basis of Accounting	23	A basis of accounting for general insurance business whereby a result is determined at the end of the accounting period reflecting the profit or loss from providing insurance cover during that period (including the anticipation of losses arising on cover to be provided in subsequent periods in respect of commitments entered into prior to the end of the accounting period) and any adjustments to the profit or loss of providing insurance cover during earlier accounting periods.
Balance Sheet Format	24	The balance sheet presented in the format required by Section B of Chapter I of Part I of Schedule 9A to the CA85. References to balance sheet asset and liability items are to the asset and liability items as specified in that format.
Bonuses	25	Amounts allocated to policyholders under with-profits contracts whose existence but not size is specified in the contract. Subject to any promises or guarantees given under the contract, bonus size and timing are at the discretion of the insurer and are determined in the light of a number of factors including past and expected investment performance during the contract. Bonuses may be regular, occasional or terminal.
Category of Business	26	Groupings of general insurance business with similar characteristics (Such as patterns of risk, claims incurrence and settlement patterns, and setting of premiums).
Claim	27	The amount payable under a contract of insurance arising from the

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		occurrence of an insured event.
Claims Handling Expenses	28	Expenses incurred in connection with the negotiation and settlement of claims. They include all internal and external expenses incurred in the handling of claims. Internal expenses include all direct expenses of the claims department and any part of the general administration expenses attributable to the claims function.
Claims Incurred	29	A claim is incurred when the event giving rise to the claim occurs. Claims incurred include paid claims and movements in outstanding claims.
Claims Incurred But Not Reported (IBNR)	30	Claims arising out of events, which have occurred by the balance sheet date but have not been reported to the undertaking at that date.
Claims Outstanding General Business	31	The amounts provided to cover the estimated ultimate cost of settling claims arising out of events which have occurred by the balance sheet date, including IBNR claims and claims handling expenses, less amounts already paid in respect of those claims.
Claims Outstanding Long Term Business	32	The amount provided to cover the estimated ultimate cost of settling claims arising out of events, which have been notified by the balance sheet date being the sums due to beneficiaries together with claims handling expenses, less amounts already paid in respect of those claims.
Coinsurance	33	An arrangement whereby two or more insurance undertakings enter into a single contract with the insured to cover a risk in agreed proportions at a specified premium.
Current Value of Investments	34	Current value means the market value determined in accordance with paragraph 25 (or, in the case of land and buildings, paragraph 26) of Part 1 of Schedule 9A to the CA85.
Deferred Acquisition Costs - General Business	35	Acquisition costs relating to the unexpired period of risk of contracts in force at the balance sheet date which are carried forward from one accounting period to subsequent accounting periods.
Deferred Acquisition Costs – Long Term Business	36	Acquisition costs relating to contracts in-force at the balance sheet date, which are carried forward from one accounting period to subsequent accounting periods in the expectation that they will be recoverable out of future margins within insurance contracts after providing for contractual liabilities.
Discounting	37	The reduction to present value at a given date of future cash flows at an assumed date by the application of an appropriate discount factor reflecting the time value of money.
Earned Premium	38	In the case of general insurance business, earned premium is the proportion of written premiums (including where relevant those of prior accounting periods) attributable to the risks borne by the insurer during the accounting period.

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Financial Reinsurance	39	Where a reinsurance contract is intended, either in whole or in part, to mitigate the requirement to establish prudent provisions, and/or to provide an element of financing, the identifiable elements of the contract which do not transfer significant insurance risk are considered to be financial reinsurance.
General Insurance Business	40	Contracts of insurance (including reinsurance) falling within one of the classes of insurance specified in Part I of Schedule 1 to the Regulated Activities Order.
Gross Premium Valuation	41	<p>A form of actuarial valuation of liabilities arising under long term insurance contracts where the premiums brought into account are the full amounts receivable under the contract. The method includes explicit estimates of cash flows for:</p> <ul style="list-style-type: none"> • premiums, adjusted for renewals and lapses; • expected claims and for with-profits business future regular but not occasional or terminal bonuses • costs of maintaining contracts; and • future renewal expenses <p>Cash flows are discounted at the valuation interest rate. The methodology for UK companies is included in FSA rules. The discount rate is based on the expected return on the assets deemed to back the liabilities as prescribed by the FSA rules. This may be further constrained by a maximum rate set by the regulator. This will be adjusted to reflect any further risks although, under this method, most of the key risks will be reflected in the modelling of the cash flows. For linked business, allowance may be made for the purchase of future units required by the contract terms and credit is taken for future charges permitted under those terms.</p>
Inception of Risk	42	In relation to general insurance business, the time at which the period of cover commences under a policy or contract of insurance.
Insurance Risk	43	Uncertainty over the likelihood of an insured event occurring, the quantum of the claim, or the time when claims payments will fall due.
Investment Return	44	Investment return comprises all investment income, realised investment gains and losses and movements in unrealised investment gains and losses. It also includes investment expenses and charges and, if appropriate, interest payable.
Linked Business	45	Long term insurance business where the benefits payable to policyholders are wholly or partly to be determined by reference to the value of, or the income from, property of any description or by reference to fluctuations in, or in an index of, the value of property of any description.
Long Term Fund	46	The fund or funds maintained by an undertaking in respect of its long-term business in accordance with the FSA rules.
Long Term Insurance Business	47	Contracts of insurance (including reinsurance) falling within one of the classes of insurance specified in Part II of Schedule 1 to the Regulated Activities Order.

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Longer Term Rate of Investment Return	48	The longer term rate of investment return is an estimate of the long term trend investment return for the relevant category of investments having regard to past performance, current trends and future expectations.
Net Premium Method	49	An actuarial valuation of liabilities arising under long term insurance contracts where the premium brought into account at any valuation date is that which, on the valuation assumptions regarding interest, mortality and disability, will exactly provide for the benefits guaranteed. A variation of the net premium method involves zillmerisation (see paragraph 81). Under the net premium method, no explicit allowance is made for the future costs of maintaining the policy but these are taken into account, if necessary, by adjusting downwards the amount of future premiums included in the calculation. For with-profits policies, vested bonuses are included in the cash flows assessed but future allocations of bonuses are not included explicitly, although they may be taken into account as a downwards adjustment to the discount rate used. The discount rate before adjustment for risk and items not explicitly included in the cash flows assessed is based on the return available on suitable investments. The detailed methodology for UK companies is included in regulations contained in the FSA rules.
Non-Participating Business	50	Long term insurance business where policyholders are not entitled to share in the surplus of the relevant long-term fund.
Non-Proportional Reinsurance	51	Contracts of reinsurance whereby the reinsurer accepts the whole or a proportion of the liability for an individual claim or group of claims incurred by the cedent in excess of an agreed amount, normally also subject to an upper limit.
Non-Technical Account	52	The section of the profit and loss account prescribed by Section B of Chapter 1 of Part 1 of Schedule 9A to the CA85 in addition to the technical accounts for general and long term insurance business.
Participating Business	53	Long term insurance business where policyholders are contractually entitled to share in the surplus of the relevant long-term fund.
Pipeline Premiums	54	Premiums written but not reported to the undertaking by the balance sheet date.
Portfolio Claims Payments	55	Amounts payable by one insurance undertaking to another in consideration for a contract whereby the latter agrees to assume responsibility for the unpaid claims incurred by the former prior to a date specified in the contract.
Portfolio Premiums Payments	56	Amounts payable by an insurer to another insurer in consideration for a contract whereby the latter agrees to assume responsibility for the claims arising on a portfolio of in-force business written by the former from a future date until the expiry of the policies.
Present Value of Future Profits ("PVFP")	57	the value determined in accordance with Rule 7.4.37 of the FSA Integrated Prudential Sourcebook and related guidance.

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Present Value of In-force Business ("PVIF")	58	The net present value of the shareholders' interest in the expected after tax cash flows from long term insurance business, on the assumption that all assets backing the business will be distributed over time to in-force policyholders and/or shareholders. The calculation of PVIF should allow for uncertainties associated with the assessment of future cashflows, as well as for the time value of money. PVIF includes both the shareholders' interest which is expected to arise in the form of cash flows over the lifetime of current in-force contracts and the interest in the surplus assets which, in practice, is not expected to be distributed over this period. This distinction is of importance when considering the application of paragraph 198 .
Proportional Reinsurance	59	A contract of reinsurance under which, in return for a proportion of the original premium, the reinsurer accepts liability for the same proportion of each related claim against the cedent.
Profit and Loss Account Format	60	The profit and loss account set out in the format required by Section B of Chapter I of Part I of Schedule 9A to the CA85. References to items in the profit and loss account are to those items as specified in that format.
Purchase Price Of Investments	61	The consideration for the purchase of investments, including related acquisition costs (eg stamp duty and brokerage) except where they are restricted by FRS 26, but excluding accrued interest included in the purchase price of interest bearing stocks. Accrued interest should be separately identified and accounted for.
Realised Investment Gains/Losses	62	<p>(a) For investments included in the financial statements at current value, the difference between the net proceeds on disposal and their purchase price.</p> <p>(b) For investments included at amortised cost, the difference between the net proceeds on disposal and the latest carrying value (or if acquired after the last balance sheet date the purchase price).</p>
Realistic value of Liabilities	63	The realistic value of liabilities being that element of the amount defined by rule 7.4.40 in the FSA's integrated prudential sourcebook, excluding current liabilities falling within the definition in rule 7.4.190, that are recognised separately on the entity's balance sheet.
Reinsurance	64	An arrangement whereby one party (the reinsurer), in consideration for a premium, agrees to indemnify another party (the cedent) against part or all of the liability assumed by the cedent under a policy or policies of insurance.
Reinsurance Inwards	65	The acceptance of risks under a contract of reinsurance.
Reinsurance Outwards	66	The placing of risks under a contract of reinsurance.
Retrocession	67	The reinsurance outwards of risks previously accepted by an insurer as reinsurance inwards. The recipient is known as the retrocessionaire. References in this Statement to reinsurance include retrocession.

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Run-Off Deviation	68	For general insurance business, the difference (before any reduction in respect of discounting) between: <ul style="list-style-type: none"> • the provisions made at the beginning of the accounting period for outstanding claims incurred in previous accounting periods, and • the payments made during the accounting period on account of claims incurred in previous accounting periods and the claims provision at the end of the accounting period for such outstanding claims.
Sale Proceeds of Investments	69	The consideration for the sale of investments after deducting the related costs of sale. In the case of interest bearing securities, the consideration should exclude any interest accrued at the date of sale.
Structured Settlements	70	Arrangements by consent between the parties concerned or under a Court Order whereby damages in the form of a lump sum are replaced by a smaller lump sum and a series of periodic payments.
Technical Account for General Business	71	The section of the profit and loss account for recording insurance business within the classes specified in Part I of Schedule 1 to the Regulated Activities Order which must be prepared in accordance with the format prescribed in Section B of Chapter I of Part 1 of Schedule 9A to the CA85.
Technical Account for Long Term Business	72	The section of the profit and loss account for recording insurance business within the classes specified in Part II of Schedule 1 to the Regulated Activities Order, which must be prepared in accordance with the format prescribed in Section B of Chapter I of Part I of Schedule 9A to the CA85.
Transaction costs (FRS 26)	73	Incremental costs that are directly attributable to the acquisition, issue or disposal of a financial instrument. An incremental cost is one that would not have been incurred if the entity had not acquired, issued or disposed of the financial instrument.
Transfer of Insurance Risk	74	A transfer of insurance risk, which may involve underwriting risk or timing risk or both, between the insured and insurer as a result of which, having regard to the commercial substance of the contract or contracts being evaluated, there are a number of reasonably possible outcomes some of which may present the insurer with the possibility of suffering a material loss.
Unearned Premiums Provision	75	This usually relates to general business and is the proportion of written premiums relating to periods of risk after the accounting date, which are deferred to subsequent accounting periods.
Underwriting Year	76	The accounting period in which a contract of general insurance incepts.

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Unexpired Risks Provision	77	The excess of the estimated value of claims and expenses likely to arise after the end of the financial year from contracts concluded before that date, insofar as their estimated value exceeds the provision for unearned premiums (after deduction of any acquisition costs deferred), and any premiums receivable under those contracts.
Unrealised Investment Gains/Losses	78	<p>The difference between the current value at the balance sheet date of investments held on that date and their purchase price. Movements in unrealised investment gains/losses comprise:</p> <ul style="list-style-type: none">• the increase/decrease in the accounting period in the value of investments held at the balance sheet date; and• the reversal of unrealised investment gains/losses recognised in earlier accounting periods in respect of investment disposals of the current period.
Written Premiums - General Business	79	Premiums, which an insurer is contractually entitled to receive from the insured in relation to contracts of insurance. These are premiums on contracts entered into during the accounting period and adjustments arising in the accounting period to premiums receivable in respect of contracts entered into in prior accounting periods.
Written Premiums - Long Term Business	80	Premiums to which the insurer is contractually entitled becoming due for payment in the accounting period.
Zillmerisation	81	A variation of the net premium method (see paragraph 49) which increases the future premiums valued to take account of acquisition costs incurred.

PART 3 - General Insurance Business

Basis of Accounting	82	Paragraphs 83 to 143 apply to general insurance contracts falling within the scope of this Statement, except those contracts, which do not satisfy the definition of an insurance contract in FRS 26 and which, in consequence, are required to be accounted for in accordance with paragraph 162 below.
	83	Underwriting results should be determined on an annual basis , notwithstanding that this will normally require some estimation to be made at the balance sheet date, particularly with regard to outstanding claims.
Gross Written Premiums	84	Written premiums should comprise the total premiums receivable for the whole period of cover provided by the contracts entered into during the accounting period, regardless of whether these are wholly due for payment in the accounting period, together with any adjustments arising in the accounting period to such premiums receivable in respect of business written in prior accounting periods.
	85	A common arrangement in general insurance is for premiums to be remitted by intermediaries on a net of commission basis to the insurer, even though the insurer is contractually entitled to the full amount. Alternatively the intermediary may remit the whole of the premium to the insurer and receive the commission as a payment. In both situations grossing up for the commission should be applied, if necessary on an estimated basis, as this correctly reflects the contractual arrangements in force. This also applies where the premiums are determined by an intermediary. Where, however, policies are issued to intermediaries on a wholesale basis and they are themselves responsible for setting the final amount payable by the insured without reference to the insurer, the written premium will normally comprise the premium payable to the insurer and grossing-up will be inappropriate unless it reflects the contractual position.
	86	Where premiums are receivable by instalments during the period of risk covered by contracts, any outstanding amount at the balance sheet date to which the insurer is contractually entitled should be treated as a debtor.
	87	Written premiums should include pipeline premiums . Contracts may have been entered into which provide for intermediaries to accept business on the insurance undertaking's behalf (for example binding covers and line-slip arrangements). The details of these policies may not be notified to the insurer until some time after the balance sheet date and may embrace business incepting both before and after the balance sheet date. The estimate of pipeline premiums should relate only to those underlying contracts of insurance where the period of cover has commenced prior to the balance sheet date.
	88	Where an insurer has offered renewal and is therefore contractually liable to pay claims if renewal is subsequently confirmed by the policyholder, it should recognise the renewal premium, subject to making a provision for anticipated lapses.

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- 89 Under some policies written premiums may be adjusted retrospectively in the light of claims experience or where the risk covered cannot be assessed accurately at the commencement of cover. Where written premiums are subject to an increase retrospectively, recognition of potential increases should be deferred until the additional amount can be ascertained with reasonable certainty. Recognition of such amounts should be commensurate with the degree to which related provisions for claims have been established. Where written premiums are subject to a reduction, an adjustment for such a reduction should be made as soon as it can be foreseen.
- 90 Additional or return premiums should be treated as adjustments to the initial premium. Where a claims event causes a reinstatement premium to be paid, the recognition of the reinstatement premium and the effect on the initial premium should reflect the respective incidence of risk attaching to those premiums in determining under the annual accounting basis that proportion earned and unearned at the balance sheet date.
- 91 Written premiums should be recognised as **earned premiums** over the period of the policy having regard to the incidence of risk. Time apportionment of the premium is normally appropriate if the incidence of risk is the same throughout the period of cover. If there is a marked unevenness in the incidence of risk over the period of cover, a basis which reflects the profile of risk should be used. The proportion of the written premiums relating to the unexpired period of these policies will be carried forward as an **unearned premiums provision** at the balance sheet date.
- Disclosure 92 The method of calculating the unearned premiums provision should be disclosed.
- Insurance Premium Taxes 93 Insurance premium taxes should not be included within written premiums in the technical account. Unpaid premium taxes should be dealt with in the balance sheet within balance sheet liabilities item GV (Other creditors including taxation and social security).
- Claims – Annual Basis 94 Provision should be made at the balance sheet date for the expected ultimate cost of settlement of all **claims incurred** in respect of events up to that date, whether reported or not, together with related claims handling expenses, less amounts already paid. There may be a considerable degree of uncertainty as to the eventual outcome of some insurance contract with a wide range of possible outcomes, and time delays in claims notifications which in some cases can exceed 25 years. If a liability is known to exist but there is uncertainty as to its eventual amount, a provision should nevertheless be made, consistent with paragraph 25 of FRS12 which deals with the role of estimates. Provision should also be made, usually on an estimated basis, for claims events which have occurred but have not yet been reported, using appropriate statistical and other techniques to address any uncertainty arising.
- 95 The level of claims provisions should be set such that no adverse **run-off deviation** is envisaged. This is consistent with the requirement of paragraph 43 of Part I of Schedule 9A to the CA85 that technical provisions should be sufficient at all times to cover any liabilities arising out of insurance contracts so far as can reasonably be foreseen. However, given the uncertainty in establishing a provision for outstanding claims, it is likely that the final outcome will prove to be different from the original liability established. In setting the provision, consideration should be given to the probability and magnitude of future experience being more adverse than assumed.

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Where there is considerable uncertainty concerning future events a degree of caution will be necessary in the exercise of the judgement required for setting provisions such that liabilities are not understated.

	96	In determining the sufficiency of evidence and the ability to measure claims costs, an insurance undertaking should take all reasonable steps to ensure that it has appropriate information with regard to its claims exposures.
	97	Paragraphs 238 to 247 set out in more detail the requirements relating to estimation techniques, uncertainty and contingent liabilities.
	98	Anticipated salvage or subrogation recoveries, where material, should be disclosed under assets item EIII (Other debtors) and not deducted from claims provisions. In accordance with Note 4 to the profit and loss account format, they should be deducted from claims incurred in the technical account for general business.
Claims Handling Expenses	99	Provision should be made at the end of the accounting period for all claims handling expenses to cover the anticipated future costs of negotiating and settling claims which have been incurred - whether reported or not - up to the balance sheet date. Separate provisions should be assessed for each category of business.
	100	In determining the provision for claims handling expenses, unless clear evidence is available to the contrary, it should be assumed that the activity of the claims handling department will remain at its current level and therefore that the contribution to its costs from future new business will remain at the same level.
	101	The provision for claims handling expenses should be included within the provision for claims outstanding but need not be separately disclosed. Claims handling expenses incurred should be included within claims incurred in the technical account for general business.
Disclosure	102	Disclosure should be made in the notes to the financial statements to provide an understanding of the main principles underlying the establishment of the claims provisions and, where relevant, any changes from previous accounting periods in the procedures adopted for establishing claims provisions, and the reasons for them. In particular there should be disclosure of the policies adopted and bases used with regard to: <ul style="list-style-type: none">- reported claims;- claims incurred but not reported;- claims handling expenses; and- salvage and other recoveries.
	103	In accordance with Note 4 to the profit and loss account format in Part 1 of Schedule 9A to the CA 85, and consistent with the requirements of FRS 12 (Provisions, contingent liabilities and contingent assets), where run-off deviations arise, the amounts should, if material, be shown in the notes to the financial statements, broken down by category. For this purpose, materiality is in relation to the insurance business as a whole and not to individual categories of insurance business.
Discounting	104	Paragraph 47(7) of Part I of Schedule 9A to the CA85 prohibits implicit discounting of claims provisions. Explicit discounting of

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claims provisions to recognise the time value of money is permissible only if the preconditions laid down in Paragraph 48 of Part I of Schedule 9A to the CA85 are satisfied, and the disclosures required by that paragraph are made. Explicit discounting will not affect the total charge to the technical account over time, but will affect the timing of the recognition of that charge.

- 105 Paragraph 48(1)(a) of Part I of Schedule 1 to Schedule 9A to the CA85 requires that explicit discounting may only be applied where the expected average interval between the date for the settlement of claims being discounted and the accounting date is at least four years. The four-year test should be applied by reference to the end of each accounting period in respect of all claims outstanding at that time, and not just once in the accounting period in which the claims were incurred.
- 106 Where applied, explicit discounting should normally be adopted by reference to **categories** of claims (with similar characteristics but not solely by length of settlement pattern) rather than to individual claims.
- 107 The calculation of the average interval referred to in paragraph **105** above should be weighted on the basis of expected claims before any deduction for reinsurance.
- 108 Discounting should be considered only if there is adequate data available to construct a reliable model of the rate of claims settlement. The principal factors to be considered are the amount of future claims settlements, the timing of future cash flows and the discount rate. A cautious approach should be taken to ensure a sufficient level of reliability in the construction of the claims settlement pattern. Procedures should be undertaken to assess the accuracy of the claims settlement pattern predicted by the model in previous periods and the current model should be adjusted, as appropriate, to reflect the out-turn and conclusions of analyses in the previous period. Cash flows should be modelled gross and net of reinsurance as reinsurance recoveries may arise later than the related claims payments.
- 109 As required by law, discounting should be applied only where assets (excluding those attributable to shareholders' funds) are available which are appropriate in magnitude and nature to cover the liabilities discounted. The discount rate must comply with the requirement of Paragraph 48(1)(e) of Part I of Schedule 9A to the CA85. In particular, it should not exceed a rate expected to be earned by assets of the undertaking which are appropriate in magnitude and nature to cover the provisions for claims being discounted during the period necessary for the payment of such claims and should not exceed either:
- a rate justified by the performance of such assets over the preceding five years; or
 - a rate justified by the performance of such assets during the year preceding the balance sheet date.
- 110 For the purpose of determining an appropriate discount rate, justification requires a consideration of the returns achieved over the period in question to the extent that this is relevant to the future.
- 111 When discounting is applied, the following disclosures should be made in the notes to the financial statements:
- the total amount of the provisions before discounting;

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- the categories of claims in relation to which discounting has been applied; and
 - for each category of claims where discounting has been applied, the methods used, the assumed average period to claims settlement, the rate of investment return used to determine the discounted value of claims provisions, and the criteria adopted for estimating the period that will elapse before the claims are settled.
- 112 The effect of the unwinding of discounted claims provisions during an accounting period should be disregarded in considering whether material adverse run-off deviations have arisen requiring disclosure under Note 4 to the Profit and Loss Account format in Section B of Chapter 1 of Part I of Schedule 9A to the CA85. (See paragraph **103** above).
- 113 Investment return associated with any unwinding of the discount on general insurance business claims provisions in an accounting period should be recorded under the headings for investment income or gains in the appropriate sections of the profit and loss account and should not be credited directly to claims incurred. Separate disclosure should then be made, where material, of the amount of the investment return which corresponds to the unwinding of the discount.
- Claims Provisions
On Acquisition
- 114 FRS 7 (Fair values in acquisition accounting) requires that, for acquisition accounting, the identifiable assets and liabilities of an acquired undertaking should be included in the acquirer's balance sheet at their fair value at the date of acquisition. In calculating the fair value of claims provisions on acquisition, consideration should be given to the amounts expected to be paid reflecting the uncertain quantum and timing of future payments.
- 115 The adjustment for the timing of payment applied in calculating the fair value of claims arising on acquisition should be treated as an element of goodwill and amortised on an appropriate basis over the run-off period of the claims arising from the portfolio of business acquired. This element of goodwill should be separately identified in the notes to the financial statements and described as "goodwill on acquired claims provisions". A review for impairment should be undertaken consistent with the requirements of FRS 11 (Impairment of fixed assets and goodwill).
- 116 The amortisation should be described as "Amortisation of goodwill on acquired claims provisions" and included under item I.8 (Other technical charges, net of reinsurance) in the technical account for general insurance business where an allocation of investment return has been made to that account from the non-technical account. Where no such allocation has been made, the amortisation should be included in item III.8 (Other charges, including value adjustments) in the non-technical account.
- Unexpired Risks
Provision
- 117 Subject to paragraph **122** below, where the estimated value of claims and expenses attributable to the unexpired periods of policies in force at the balance sheet date exceeds the unearned premiums provision in relation to such policies after deduction of any acquisition costs deferred, an **unexpired risks provision** should be established. If material, this provision should be disclosed separately either in the balance sheet or in the notes to the financial

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- statements. This is consistent with the requirements of FRS 12 on onerous contracts.
- 118 An assessment of whether an unexpired risks provision is necessary should be made for each grouping of business, which is managed together with any unexpired risks surpluses and deficits within that grouping being offset. For this purpose “managed together” is to be construed in accordance with paragraph 119 below.
- 119 Business should only be regarded as being managed together where no constraints exist on the ability to use assets held in relation to such business to meet any of the associated liabilities and either:
- (i) There are significant common characteristics, which are relevant to the assessment of risk and setting of premiums for the business lines in question; or
 - (ii) the lines of business are written together as separate parts of the same insurance contracts.
- 120 For binding authorities, where the insurer is unable to influence the terms on which policies are issued, a provision should be established at the balance sheet date for any anticipated losses arising on policies incepting in the period after the balance sheet date during which the binding authority entered into before that date remains in force.
- 121 The assessment of whether an unexpired risks provision is required and if so its quantum should be based on information available at the balance sheet date which may include evidence of relevant previous claims experience on similar contracts as adjusted for known differences, events not expected to recur and, where appropriate, the normal level of seasonal claims if the previous accounting period was not typical in this respect. The assessment should not however take into account any new claims events occurring after the balance sheet date as, these are non-adjusting events. Exceptional claims events, however, occurring between the balance sheet date and the date on which the financial statements are approved by the board of directors should be disclosed in the notes to the financial statements together with an estimate of their financial effect. The amount of any unexpired risks provision should be determined having regard to paragraph 43 of Schedule 9A to the CA85 which requires technical provisions to be sufficient at all times to cover any liabilities arising out of insurance contracts so far as can reasonably be foreseen. Where there is considerable uncertainty concerning future events, a degree of caution will be necessary in the exercise of the judgement required for setting provisions such that liabilities are not understated.
- 122 In calculating the estimated value of future claims in relation to the unexpired periods of risk on policies in force at the balance sheet date, the future investment return arising on investments supporting the unearned premiums provision and the unexpired risks provision may be taken into account. For the purposes of calculating this provision, the deferred acquisition costs should be deducted from the unearned premiums provision. The investment return will be that expected to be earned by the investments held until the future claims are settled.
- 123 Acquisition costs to which the provisions of Schedule 9A to the CA85 on deferral apply, should not be written off in whole or in part to the profit and loss account as being irrecoverable for the purpose of reducing or eliminating the need for an unexpired risks provision.
- 124 Disclosure should be made of the method of assessing any

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requirement for an unexpired risks provision and, in particular, the practice with regard to recognising future investment return, offsetting surpluses and deficits and the extent to which post balance sheet events are taken into account.

Equalisation Reserves	125	Disclosure should be made in the accounting policies section of the financial statements where an equalisation reserve has been established in accordance with Chapter 6 of FSA rules. Where, in accordance with Note 24 to the balance sheet format in Schedule 9A to the CA 85, equalisation reserves are included under balance sheet liabilities item C.5 (Equalisation provision), the following disclosures should be made in the notes to the financial statements: <ul style="list-style-type: none">- the amounts provided are not liabilities because they are in addition to the provisions required to meet the anticipated ultimate cost of settlement of outstanding claims at the balance sheet date; and- notwithstanding this, they are required by Schedule 9A to the CA 85 to be included within technical provisions.
	126	In addition, there should be disclosure of the impact of equalisation reserves on shareholders' funds and the effect of movements in the reserves on the results of the accounting period. Where earnings per share figures are disclosed, consideration should be given to disclosure of an alternative earnings per share figure disregarding equalisation reserves.
Portfolio Premiums And Claims	127	Portfolio premiums payable should be included within premiums for reinsurance outwards in the financial statements of the transferor undertaking but deferred to subsequent accounting periods as appropriate in respect of any unexpired period of risk at the balance sheet date. In the financial statements of the transferee undertaking they should be included with written premiums with any amount unearned at the balance sheet date being carried forward in the unearned premiums provision.
	128	Portfolio claims transfers should be accounted for in the financial statements of the transferor undertaking as payments in settlement of the claims transferred in accordance with the requirements of Note 4 to the profit and loss account format.
	129	For the same reason, the consideration receivable by the transferee undertaking should be credited to claims payable in the balance sheet.
	130	Disclosure should be made in notes to the financial statements of any claims portfolio transfers, which materially affect the transferee undertaking's exposure to risk.
Structured Settlements	131	Where, pursuant to a structured settlement arrangement falling within one of the cases referred to in Section 329AA of the Income and Corporation Taxes Act 1988, either: <ul style="list-style-type: none">• an annuity is purchased by a general insurance undertaking under which the structured settlement beneficiary is the annuitant; or• an annuity previously purchased by a general insurance undertaking for its own account to fund the periodic payments under a structured settlement agreement is assigned to the structured settlement beneficiary;

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the general insurance company will normally remain liable to the policyholder should the annuity provider fail. Unless this is not the case, this liability should continue to be recognised in the balance sheet. An annuity, paid by an annuity provider, which exactly matches the amount and timing of this liability should be recognised as an asset and measured at the same amount as the related obligation.

Deferred Acquisition
Costs

- 132 **Acquisition costs** should be deferred commensurate with the unearned premiums provision. The acquisition costs to be deferred will be that proportion of the total acquisition costs which the unearned premiums provision bears to gross written premiums for the class of business in question. For this purpose acquisition expenses should be allocated to classes of business. This may not always be possible for reinsurance business inwards since the ceding enterprise, when advising the reinsurer of the unearned premium provision, may include in that provision an amount for deferred acquisition expenses. In these circumstances, an estimate should be made.
- 133 Advertising costs should not be deferred unless they directly relate to the acquisition of new business.
- 134 **Deferred acquisition costs** should be shown separately in the balance sheet under assets item GII (Deferred acquisition costs).
- 135 Related reinsurance commissions deferred should not be netted against deferred acquisition costs but should be shown under balance sheet liabilities item H (Accruals and deferred income).

Insurance Business
In Run off

- 136 the provisions of FRS 3 (Reporting financial performance) should be applied where a decision has been taken to cease writing the whole, or a material category, of the insurance business. For this purpose a material category must constitute a discrete segment of the insurance business.
- 137 Subject to paragraph **138**, provision should be made for the full amount of any costs associated with running off the insurance business no longer being written. Full provision for these additional costs should be made in the accounting period in which the decision to cease writing new business is taken. No part of this additional expenditure should be charged in future accounting periods against the results of other new business.
- 138 In setting any additional provision for the costs of running off the insurance business no longer being written, the amount provided should comply with the FRS 3 requirement that obligations that have been incurred should be recognised to the extent that they are not expected to be covered by the future profits of the operation. Thus, expected future investment return not already recognised in calculating technical provisions should be taken account of (except to the extent that an asset would be created) with separate disclosure in the notes to the financial statements of the full amount of the additional provision required and of the expected future investment return which has been offset against it. Investment Return should be recognised as that which is expected to be earned on the assets of the business prior to settlement in future accounting periods of the undiscounted claims liabilities and expense provisions of the business no longer being written.
- 139 The principles to be applied in providing for claims are unaltered by a partial or complete cessation of writing new business. The

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provision will need to include any additional claims handling costs arising as a result of ceasing wholly or partly to write new business (for instance, the costs where relevant of scaling down or closing the claims handling department). Other significant additional costs may include redundancy and similar payments (other than in relation to claims handling staff), continuing administrative costs and the additional costs of making recoveries under reinsurance contracts.

Deferred Taxation
(Section 107
Finance Act 2000)

- 140 Where general insurance claims provisions recorded in tax computations exceed the amount that would have been provided on the basis of full foresight, and discounting at the rate required by tax legislation, HM Revenue and Customs (HMRC) may raise an additional charge to compensate it for the deferral of any tax payment arising as a result.
- 141 The additional charge referred to above is raised through the tax charge to compensate HMRC for receiving tax later than would have been the case if the circumstances in paragraph **140** had not applied. It should therefore be regarded as a permanent difference and recorded as part of the tax charge for the accounting period to which it relates.
- 142 Where non-life insurance technical provisions included in tax computations are less than the amount of the related claims when determined under Section 107 Finance Act 2000, that section requires HMRC to make an adjustment in favour of the taxpayer calculated by reference to that difference. Where in the accounting period there is an excess of this credit (“finance credit”) over any charge (“finance charge”) referred to in paragraph **140** above, this should be treated as a permanent difference and credited to the tax charge.
- 143 Where general insurance technical provisions disclosed in the financial statements exceed the amount used for tax computational purposes, a deferred tax asset should be established, as taxable profits will exceed accounting profits. This asset will be recognised subject to compliance with the relevant accounting standard.

PART 4 - Long Term Insurance Business

Scope	144	Except in the case of contracts issued by insurance undertakings falling within the scope of FRS 26 which do not satisfy the definition of an insurance contract or contain a discretionary participation feature and with-profits life insurance business which, by virtue of falling within the scope of the FSA realistic capital regime, is subject to paragraph 4 of FRS 27, paragraphs 163 to 217 will apply in full.
	145	<p>Where and to the extent that an insurance undertaking carries on with-profits life insurance business falling within the scope of FRS 27, the following provisions of the SORP are superseded by the requirements of FRS 27:</p> <ul style="list-style-type: none">• Paragraph 170 to 177 (deferred acquisition costs)• Paragraphs 180 to 183 (determination of the long term business provision)• Paragraph 185 (allowance for future bonuses) insofar as future bonuses are recognised in the calculation of the realistic liabilities• Paragraph 186 (net premium method)• Paragraph 196 (exclusion of certain regulatory margins from the long term business provision);
	146	However, non-participating life insurance contracts written within, or by a subsidiary or associate of, a with-profits fund subject to FRS 27 will be subject to paragraphs 163 to 217 of this statement if they fall to be accounted for as insurance contracts, and paragraphs 158 to 162 will apply if under FRS 26 they are required to be accounted for as investment contracts.
	147	Paragraphs 148 to 157 apply to the measurement of the with-profits liabilities and related assets of with-profits contracts falling within the scope of FRS 27.
FRS 27	148	Paragraph 4(a) of FRS27 requires that 'for with-profits funds falling within the scope of the FSA realistic capital regime, liabilities to policyholders arising from with-profits life assurance business shall be stated at the amount of the realistic value of liabilities adjusted to exclude the shareholders' share of projected future bonuses'. The amount deducted should not exceed the amount included in the liability. The FSA's realistic capital regime permits insurers to use a range of approaches when calculating liabilities within the realistic balance sheet. Some of these incorporate explicit projection of bonuses and the corresponding shareholder transfers whilst others rely on retrospective calculations of amounts earned by with profits policyholders. However, independent of the mechanism used to calculate the liabilities, the philosophy underpinning the FSA's approach is that these liabilities should represent the value of the fund's total liabilities for with profits business,

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including the value of future transfers to shareholders, calculated using financial assumptions consistent with the market pricing of financial instruments.

- 149 To ensure consistency with this, the shareholders' share of projected future bonuses deducted in accordance with Para 4(a) should be calculated as the value of future transfers to shareholders calculated using market consistent financial assumptions, and assuming that transfers take place at a level consistent with the assumptions within the FSA realistic balance sheet. Where an explicit assumption is not required in order to calculate the liabilities under the FSA's approach then continuation of the current profit sharing arrangements should be assumed unless the firm has plans to change this approach. Non-economic projection assumptions should be consistent with those used elsewhere in the realistic balance sheet. The amount deducted in accordance with this paragraph should be taken to the fund for future appropriations. If shareholders transfers have been included as part of the FSA realistic liability (or otherwise included in liabilities) then the amount of such transfers should be taken out of liabilities and included in the FFA, together with any related tax liability. If shareholders transfers have not been set up as part of the FSA realistic liability or elsewhere, no adjustment is required.
- 150 Paragraph 4(b) of FRS 27 (acquisition costs not to be deferred) does not apply to insurance funds falling outside the scope of the FSA realistic capital regime.
- 151 Paragraph 4(d) of FRS 27 permits an amount to be recognised for the **present value of future profits** (PVFP) on non-participating business written in a with profits fund when the non-participating business is: (i) measured on this basis for the purposes of the regulatory returns made under the FSA realistic capital regime, (ii) the value of the PVFP is calculated on the basis used in the FSA's realistic capital regime and (iii) the determination of the realistic value of liabilities takes account of this value either directly or indirectly. As explained in paragraph 13 of FRS 27 in determining whether the PVFP of non-participating business has been taken into account in determining the realistic liabilities it is not necessary that there is a direct link between the value of the realistic liabilities and the value of the PVFP. Where with profits policyholders are entitled to a share of the profits on non-participating business it would generally be expected that the determination of the realistic liabilities would take account, directly or indirectly, of the value of future profits on this business.
- 152 Paragraph 4 of FRS 27 requires that the value of the PVFP asset recognised should be determined in accordance with the FSA's realistic capital regime requirements. Paragraph 15 of FRS 27 explains that the value calculated under the realistic capital regime requirements must be adjusted to ensure consistency where adjustments have been made onto the MSSB measurement basis in relation to non-participating contracts. The measurement of the PVFP asset recognised in accordance with the FSA's realistic regime may take into account the release of capital requirements for non-participating business. It would not be appropriate to

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recognise this release of capital requirements within the PVFP asset presented in the accounts because the MSSB liabilities do not include an allowance for capital. Therefore the amount of the PVFP asset determined for the purposes of the FSA's realistic capital regime should be adjusted accordingly.

- 153 For entities within the scope of FRS 26 the profit recognition profile for non-participating contracts which do not satisfy FRS 26's definition of an insurance contract or contain a discretionary participation feature will be determined by the requirements of that Standard and the guidance relating thereto in paragraphs **159** to **162** of this Statement. Where these contracts are written in a with profits fund, paragraph **151** will apply but the PVFP value recognised for such contracts for the purposes of the FSA's realistic capital regime should be adjusted to reflect the difference in the profit recognition bases between the basis used to determine the PVFP value used in the FSA's realistic capital regime and the profit recognition profile determined by FRS 26 and FRS 5.
- 154 Paragraph 4(e) of FRS 27 permits that where a with profits fund has an interest in a subsidiary or associated entity that is valued for FSA regulatory purposes at an amount in excess of the net amounts that would be included in the entity's consolidated accounts, an amount may be recognised representing this excess if the determination of the realistic value of liabilities to with-profits policyholders takes account of this value. As explained in Paragraph 16 of FRS 27 this situation could arise where the subsidiary or associated entity writes non-participating business and the value of the subsidiary or associated entity recognised for FSA reporting purposes incorporates the PVFP of non-participating business written in the subsidiary or associated entity. The value of the subsidiary or associated entity recognised for FSA reporting purposes is reduced by the subsidiary's or associate's capital requirement as noted in rule 7.4.33(3) of the FSA's integrated prudential sourcebook. When preparing both consolidated and non-consolidated accounts, the excess value that may be recognised should therefore be taken as the excess before deduction of the subsidiary or associated entity's capital requirement.
- 155 Paragraph 5 of FRS 27 permits a number of options for how the amounts recognised in paragraphs **152** to **154** should be presented. In order to comply with the requirements of CA 85 Schedule 9A the option in 5(a) should be adopted but if this is not feasible, the option in 5(c) should be applied.
- 156 Paragraph 56(a) of FRS 27 requires disclosure of the effect of changes in assumptions used to measure life assurance liabilities. The effect of each change in assumptions having a material effect on the group must be shown separately subject to paragraph 59 which permits the impact of changes in assumptions which have a common cause to be grouped together. The impact of changes in assumptions which individually do not have a material effect on the group may be disclosed in aggregate. A narrative description of these should be provided. Where it is not practicable to refer to each change in assumption individually, this should analyse

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		the impact in a way that meets the objective of the disclosure and is appropriate for the entity's particular circumstances.
	157	Where an assumption is linked to a defined external variable, for example base rates, a change in that variable will not constitute a change in assumptions. Its impact should therefore be categorised under paragraph 56(c) of FRS 27 as a change resulting from external development.
FRS 26	158	Paragraphs 159 to 162 apply to contracts issued by insurance undertakings that fall to be accounted for as investment contracts under FRS 26.
	159	Where the consideration for the investment contract issued comprises both a fee for the origination of a financial instrument and an ongoing charge for the provision of investment management services, the insurance undertaking should record the origination fee as turnover on the date on which it becomes entitled to it where it can be demonstrated that the undertaking has no further obligations in respect of the fee.
	160	Subject to this, origination fees and charges for managing investments should be recognised as revenue where and to the extent that the insurance undertaking has obtained the right to consideration through its performance.
	161	Incremental costs that is directly attributable to securing an investment management contract are recognised as an asset if they can be identified separately and measured reliably and if it is probable that they will be recovered. An incremental cost is one that would not have been incurred if the entity had not secured the investment management contract. The asset represents the entity's contractual right to benefit from providing investment management services and is amortised as the entity recognises the related revenue. If the entity has a portfolio of investment management contracts, it may assess their recoverability on a portfolio basis.
	162	As noted in Paragraph C26 of Appendix C to FRS 26, deposit accounting should be adopted for investment contracts. This involves the following: <ul style="list-style-type: none"> (a) One party recognises the consideration received as a liability rather than as revenue. (b) The other party recognises the consideration paid as a financial asset rather than as an expense.
Gross Premiums Written	163	Premiums, including those for inwards reinsurance business, should be accounted for when due for payment. Where the amount due is Not known, for example with certain pensions business, estimates should be used. For unit-linked business the due date for payment may be taken as the date when the liability is established.
Reinsurance Outwards	164	Reinsurance outwards premiums should be accounted for when paid or payable.
Disclosure	165	The basis of premium recognition should be disclosed in the financial statements.

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Claims Recognition	166	Claims payable on maturity should be accounted for when the claim becomes due for payment and claims payable on death should be accounted for on notification. Where a claim is payable and the policy or contract remains in force, the relevant instalments should be accounted for when due for payment. In all cases there should be consistent treatment between the recognition of the claim in the technical account for long-term business and the calculation of the long-term business provision and/or the provision for linked liabilities as appropriate. In accordance with Note 21 to the balance sheet format, provision for claims incurred but not reported (IBNR), including related claims handling expenses, should be included within balance sheet liabilities item C2(a) (Long term business provision). Any element of the claims payable which represents bonus allocated in anticipation of the surplus arising from the actuarial valuation at the balance sheet date should be included in line 5(a) (Claims paid) of the technical account for long term business.
Surrenders	167	Surrenders should be included within claims incurred and accounted for either when paid or at the earlier date on which, following notification, the policy ceases to be included within the calculation of the long term business provision and/or the provision for linked liabilities. Any element of surrenders payable which represents bonus allocated in anticipation of the surplus arising from the actuarial valuation at the balance sheet date should be included in item 5(a) (Claims paid) of the technical account for long term business.
Claims Handling Expenses	168	Claims incurred should include related internal and external claims handling expenses.
Disclosures	169	The basis of claims recognition should be disclosed.
Deferred Acquisition Costs	170	Paragraph 12 of Part I of Schedule 9A to the CA85 requires costs associated with the acquisition of new business incurred in an accounting period but relating to subsequent accounting periods to be deferred Acquisition costs should be deferred explicitly. The deferred acquisition costs asset may be calculated in whole or in part by means of an actuarial method, which enables the costs so deferred to be separately identified.
	171	Advertising costs should not be deferred unless they directly relate to the acquisition of new business.
	172	The full amount of the deferred acquisition costs should be included in balance sheet assets item G11 (Deferred acquisition costs), after adjusting, where appropriate, for any deferred tax liability recognised automatically in the actuarial valuation. A deferred tax provision should be established where appropriate in accordance with the requirements of current accounting standards. The long-term business provision should be adjusted appropriately to reflect the inclusion of the deferred acquisition costs asset and any corresponding deferred tax liability.
	173	The movement in the accounting period in deferred acquisition costs disclosed, as an asset should be included under item 8(b) (Change in deferred acquisition costs) of the technical account for long-term business.
	174	Deferred acquisition costs, which are carried forward, should be

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amortised over a period no longer than that in which, net of any related deferred tax provision, they are expected to be recoverable out of margins in matching revenues in relation to the related insurance contracts in force at the balance sheet date, at a rate, which is commensurate with the pattern of such margins.

- 175 Acquisition costs should not be deferred to the extent that:
- the costs in question have already been recovered (for example where the design of the policy provides for the recovery of costs as incurred);
 - the net present value of margins within the insurance contracts is not expected to be sufficient to cover deferred acquisition costs after providing for contractual liabilities to policyholders and expenses; or
 - the receipt of future premiums or the achievement of future margins is insufficiently certain based on estimates of future expected discontinuance rates or other experience.
- 176 Deferred acquisition costs should be reviewed by category of business at the end of each accounting period. Where circumstances which have justified the deferral of such costs no longer apply or are considered doubtful, the costs to the extent to which they are considered to be irrecoverable, should be written off to the long-term business technical account.
- 177 The basis of amortising acquisition costs should be disclosed in the notes to the financial statements.

Technical Provisions

- 178 Under Schedule 9A to the CA85, technical provisions in respect of long term business are analysed as follows:-
- Long term business provision;
 - Technical provisions for linked liabilities; and
 - claims outstanding.

Balance sheet liabilities item C4 (Provision for bonuses and rebates) and line II.7 (Bonuses and rebates, net of reinsurance) in the technical account for long-term business should not be used. Bonuses attributable to the accounting period, other than those included within claims paid in accordance with paragraphs **166** and **167**, should be included in line II.6 (a) (Change in other technical provisions - long term business provision) and in Balance Sheet Liabilities item C.2 (Long term business provision).

Long Term Business Provision

- 179 Paragraph 46(3) of Part I of Schedule 9A to the CA85 requires the computation of the LTBP of UK business to be made annually by a Fellow of the Institute or Faculty of Actuaries on the basis of recognized methods, with due regard to the actuarial principles laid down in the EU Third Life Directive (92/96/EEC).
- 180 The **gross premium method** should be used for every class of insurance business except those for which the net premium method is used in the related regulatory returns, but policyholder liabilities of overseas subsidiaries may be computed on a local basis subject to paragraph **202**.

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- 181 The method of valuation used for each principal category of insurance business should be disclosed in the notes to the accounts together with a summary of the principal assumptions made in accordance with paragraph **184**. In the case of overseas subsidiaries, the computation shall be prepared by an actuary or other specialists using recognized actuarial methods. Guidance on the extent to which the local bases of reporting can be incorporated in group accounts is contained in paragraph **202**. Paragraph 43 of Part I of Schedule 9A to the CA85 requires the long term business provision to be at all times sufficient to cover any liabilities arising out of insurance contracts as far as can reasonably be foreseen.
- 182 Liabilities should be assessed on a basis consistent with the bases adopted for valuing the corresponding assets. In determining the long-term business provision and the technical provision for linked liabilities, no policy may have an overall negative provision except as allowed by FSA rules or a provision, which is less than any guaranteed surrender or transfer value.
- 183 Having regard to the adjustment referred to in paragraph **172** and the need for consistency in paragraph **182**, the long term business provision may be calculated on the basis used for reporting under FSA rules subject to:
- Reassessment of the provisions and reserves included in the statutory liabilities for solvency purposes to consider the extent to which they should be included in the long-term business provision. This will require the exclusion of the appropriate proportion of reserves (such as investment reserves, reserves to cover general contingencies and reserves to cover the specific contingency of the fund being closed to new business). Any amount in excess of the necessary provision should be disclosed in the financial statements as a reserve or in the fund for future appropriations as appropriate;
 - The reversal of any reduction in policyholder liabilities in the regulatory returns where these liabilities already implicitly take account of a pension fund surplus through future expense assumptions, which reflect, lower expected contributions.
- 184 Paragraph 46(2) of Part I of Schedule 9A to the CA85 requires that a summary of the principal assumptions underlying the long-term business provision should be given. This would include for each principal category of business the more significant assumptions relating to the following:
- premiums;
 - persistency;
 - mortality and morbidity;
 - interest rates;
 - the discount rates used with, if relevant, explanation of the basis of reflecting risk margins; and
 - if applicable, any other significant factors.
- There should be a brief discussion (which may be qualitative) of:
- any changes in significant assumptions or bases of preparation; and

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- the sensitivity of the amount reported with respect to changes in the principal assumptions or bases of preparation.

(See also the disclosure requirements in paragraph **240**.)

	185	For each significant class of with-profits insurance business, the insurer should disclose the extent to which the basis of preparation of the long-term business provision incorporates allowance for future bonuses. For example, it should be stated (if it is the case) that explicit provision is made only for vested bonuses (including those vesting following the current valuation) and that no such provision is made for future regular or terminal bonuses. If practical, and it can be done without undue cost, insurers should disclose the amount that has been included explicitly in the long-term business provision in relation to future bonuses. If the valuation method makes implicit allowance for future bonuses by adjusting the discount rate used or by another method, this fact should be stated together with a broad description of the means by which such allowance is made.
	186	Where the valuation is performed using a net premium method, bonuses should be included in the long-term business provision only if they have vested or have been declared as a result of the current valuation.
	187	The aggregate of the bonuses added to policies in the accounting period should be disclosed by way of note to the financial statements.
	188	Where the long-term business provision has been determined on an actuarial basis that, in assessing the future net cash flows, has regard to the timing of tax relief where assumed expenses exceed attributable income, the entity should ensure that such tax relief is excluded from the determination of any deferred taxation requirement.
	189	Where the technical provision for linked liabilities has regard to the timing of the tax obligation, the effect of this should be excluded from the determination of any deferred tax requirement.
Technical Provisions for Linked Liabilities	190	The relevant provision for any contract should not be less than the element of any surrender or transfer value which is calculated by reference to the relevant fund or funds or index.
	191	The net assets held to cover linked liabilities at the balance sheet date may differ from the technical provisions for linked liabilities. The reasons for any significant mismatching should be disclosed. In practice this should apply only to overseas companies included in group financial statements because of the requirements of PRU 4.2.57 of the FSA rules.
Claims Outstanding	192	Amounts included under balance sheet liabilities item C3 (claims outstanding) should include claims in relation to both linked and non-linked business.
Fund for Future Appropriations	193	Note 19 to the balance sheet format defines the fund for future appropriations as an item comprising all funds the allocation of which either to policyholders or to shareholders has not been determined by the end of the financial year.
	194	In the case of funds where there is reasonable certainty over the allocation to policyholders or to shareholders of all items recognised in the technical account for long term business, it is inappropriate to

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		establish a fund for future appropriations. However, certain long-term business funds of proprietary insurers are established in such a way that segmentation between shareholders' reserves and policyholders' liabilities is not clear cut.
	195	Where a fund for future appropriations is established, the notes to the financial statements should indicate the reasons for its use and the nature of the funds involved.
Reserves Relating to Long Term Business	196	Investment reserves (realised and unrealised investment gains and exchange gains), surpluses carried forward, resilience and similar reserves, contingency and closed fund reserves which may be included in the statutory liabilities for solvency purposes under the FSA rules, should be considered to assess the extent to which they should be included in the long term business provision (see paragraph 183).
	197	The investment return (which includes movements in realised and unrealised investment gains and losses) and related tax charges on assets representing reserves which are held within the long term fund for solvency purposes under the FSA rules should be credited to the technical account for long term business. Allocations may then be made as appropriate to the non-technical account in accordance with paragraphs 292 and 293 or to the fund for future appropriations.
Present Value of Acquired In-Force (PVIF) Business	198	Consistent with FRS 6 (Acquisitions and mergers) and FRS 7 (Fair values in acquisition accounting), the PVIF arising from the acquisition of a portfolio of long term insurance business should be recognised in the balance sheet as an asset. Subject to paragraph 201 below, the relevant element of the asset should be amortised and the discount unwound over the anticipated lives of the related contracts in the portfolio on a systematic basis. The relevant element is that part of PVIF which will be recognised as profit over the remaining lifetime of the in-force policies. The carrying value of the asset should be tested annually for impairment, as per paragraph 115 .
	199	Internally generated PVIF should not be recognised.
	200	The amortisation should be included in the technical account for long-term business under item II.11 (Other technical charges, net of reinsurance) and the amount of the PVIF asset and the amortisation for the accounting period should be disclosed separately. Disclosure should also be made of the method of amortisation employed.
	201	Where a group reconstruction occurs and the new group carries on substantially the same insurance business as the group which it replaces (for example where a demutualisation is effected through the establishment of a proprietary company to acquire the business of an existing mutual insurer), any PVIF which would be regarded as internally-generated under the former group structure should continue to be treated as such in the new group.
Overseas Subsidiaries	202	Paragraph 40 of FRS2 requires uniform accounting policies to be used in determining the amounts to be included in consolidated financial statements, if necessary by making consolidation adjustments of amounts reported by subsidiaries. However policyholder liabilities of overseas subsidiaries incorporated into group financial statements may be computed on a local basis (either on a regulatory basis or in accordance with generally accepted

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accounting principles) provided the principles outlined in this SORP are followed and this is not inconsistent with paragraph 40 of FRS 2. Disclosure of that fact should be made in the notes to the group financial statements.

- 203 Paragraph 41 of FRS 2 recognises that in exceptional cases different accounting policies may be used when consolidating subsidiaries. Where the directors of the parent undertaking depart from the CA85 general requirement to use the same group accounting rules, or otherwise determine the assets or liabilities to be included in the consolidated financial statements, the CA85 requires disclosure of the particulars, which would include the different accounting policies used.
- Deferred Tax
- 204 Deferred tax provisions, including deferred tax provided in relation to unrealised investment gains, should be shown separately under liabilities item E2 (Provisions for other risks and charges – provision for taxation) of the balance sheet format. Any net deferred tax asset should be shown as a separate sub-heading within assets EIII (Debtors – other debtors).
- 205 In the case of a composite insurance company or group, any policy to discount deferred tax should be applied to the whole of the insurer's business, including both the long term insurance business and the general insurance business and other shareholders' interests.
- 206 Timing differences can arise between the recognition of profits in the accounts and the emergence of surplus on the basis required by the FSA rules on which the taxation of the profits of life assurance business is currently based. In respect of such timing differences, the general incremental liability principle underlying FRS19 should be applied and deferred tax should be recognised as a liability or asset only if the transactions or events that give the insurer an obligation to pay more tax in future or a right to pay less tax in future have occurred by the balance sheet date.
- 207 It follows that where payment of incremental tax in the future depends upon a specific future event under the undertaking's control no event giving rise to the need to provide deferred tax has occurred. An example of this may be where an insurer has made arrangements under which part of the long-term fund is identified as being referable solely to shareholders resulting in the amount attributed and the movement thereon being recognised in the profit and loss account. In these circumstances no additional deferred tax should be recognised if the reversal of the timing difference is dependent solely on the discretion of the undertaking in bringing an amount into account as an increase or decrease in the value of non-linked assets in the revenue account required by Rule 9.14(b) of FSA rules. However, the amount of any deferred tax not recognised on such a timing difference should be disclosed in the notes to the accounts in accordance with paragraph 64(e) of FRS 19. This amount should be determined using the incremental rate of tax applicable to additional surplus in future years using enacted tax rates and legislation, but otherwise assuming that the existing basis of taxation of the undertaking is maintained.
- 208 The reconciliation required by paragraph 64(a) of FRS19 should apply only to the tax charge borne by shareholders through the non-technical account.

Disclosure of Tax

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Provisions	209	To the extent that they are not allowed for in the computation of the long term technical provision or the provision for linked liabilities, tax provisions should be included within liabilities item GV (Creditors – other creditors including taxation and social security) of the balance sheet format and disclosed either as a separate sub-category of that item or in the notes to the financial statements.
Grossing-up for Tax	210	Where the shareholders' profit from long term business is computed on an after-tax basis, it should be grossed-up to the pre-tax level for presentation in the non-technical account section of the profit and loss account. This grossing-up should be at the effective rate in accordance with FRS16 (Current tax). Uniquely, for life insurance business there is a single tax charge which integrates tax on both shareholders' profits and policyholders' investment return. Any disclosure of an amount as tax on shareholders' profits alone is therefore notional. Accordingly, for this business it will normally be appropriate to take the full rate of corporation tax as the appropriate rate to be attributed to shareholders' profits for the accounting period in question provided this does not result in material mis-statement of the profit before tax for the year.
	211	Where shareholders' profits from long term business are computed at the pre-tax level, no grossing-up is required although, where transfers from the fund are partly on this basis and partly on an after-tax basis, the after-tax figure should be grossed up.
	212	Tax attributable to the long-term business should be shown at line 11a (Tax attributable to long term business) of the technical account for long-term business. The tax attributable to the balance on the long-term business technical account should be included in line 2a (Tax credit attributable to balance on long term business technical account) of the non-technical account. The tax charge in line 9 of the non technical account (Tax on profit or loss on ordinary activities) will then comprise the shareholders' tax charge on all activities carried on by the undertaking.
Segmental Reporting	213	In the case of long term insurance business, segmental analysis should be provided of gross new business premiums and, if materially different, new business premiums net of reinsurance. New annual and single premiums should be disclosed separately in the financial statements together with an explanation of the basis adopted for recognising premiums as either annual or single premiums. New annual premiums should be shown as the premiums payable in a full year ie annual equivalent premium.
	214	For the purpose of paragraph 213 above, new life insurance premiums must be defined in accordance with the following principles: 'Single premium contracts shall consist of those contracts under which there is no expectation of continuing premiums being paid at regular intervals. Additional single premiums paid in respect of existing individual contracts shall be included. Regular premium contracts shall include those contracts under which premiums are payable at regular intervals during the policy year, including repeated or recurrent single premiums where the level of premiums is defined'. The words in quotation marks are taken from paragraphs 2 and 3 of the instructions for completing Form 47 in the FSA rules.
	215	In addition, FSA guidance states that:

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'It is typical of regular premium business that the office will issue a renewal notice for the expected amount of the premium, albeit that the policyholder may have a contractual right to pay a different amount, or nothing at all. Another characteristic might be that premiums collection is by direct debit or other payment order'.

- 216 DSS rebates received on certain pensions contracts should be treated as single premiums.
- 217 Internal transfers between products where open market options are available should be counted as new business. If no open market option exists, the transfer should not be treated as new business.

PART 5 - General and Long Term Insurance Business

Commission	218	Paragraph 78 of Part I of Schedule 9A to the CA85 requires disclosure of the total amount of commissions for direct business including acquisition, renewal, collection and portfolio management. For this purpose, commission should exclude payments made to employees of the undertaking.
Exchange Gains and Losses	219	Where SSAP 20 (Foreign currency translation), or FRS 23 (The Effects of Changes in Foreign Currency Exchange Rates) insofar as it applies to entities writing insurance business, require companies to include exchange differences within the profit and loss account, these differences should be dealt with through the non-technical account except for long term insurance business where exchange differences should be recorded in the technical account for long term business. Where the assets and liabilities of an insurance enterprise are denominated mainly in a foreign currency, SSAP 20/FRS 23 requires that the closing rate/net investment method of translating the local currency financial statements should normally be used. Under the closing rate/net investment method of foreign exchange translation, exchange differences arising from the retranslation of the opening net investment in a foreign enterprise at the closing rate of exchange should be recorded as a movement in reserves except where, in the case of the long term insurance business, it is more appropriate to take them to the fund for future appropriations.
Segmental Reporting	220	For individual financial statements (but not group financial statements), the disclosures required by paragraphs 75 to 77 of Part 1 of Schedule 9A to the CA85 should be made. Segmented analysis should also conform with the requirements of SSAP25 (Segmental Reporting).
Guarantee Fund Levies Based on Premium Income	221	Levies based on premium income represent a charge on the Insurance undertaking even if they are passed on to policyholders in higher premiums. They should therefore be included in the profit and loss account as an expense and not as a deduction from written premiums. General business levies raised by the Financial Services Compensation Scheme (FSCS) and levies raised by the Motor Insurers' Bureau should be included within item 7(c) (Administrative expenses) in the technical account for general business. Long term business levies raised by the FSCS should be included within item 8(c) (Administrative expenses) in the technical account for long term business. FSCS levies are raised by reference to "financial years" of the Scheme ending on 31 March and are based on the leviable premium income of the calendar year ending immediately before the beginning of the Scheme's financial year, so for example a levy raised in the Scheme's financial year ending 31 March 2003 would be based on the leviable premium of the 2001 calendar year.
	222	<p>In deciding whether a provision for guarantee fund levies should be made, it will be necessary in accordance with FRS 12 to determine whether:</p> <ul style="list-style-type: none">• the entity has a present obligation as a result of a past event;

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- it is probable that a transfer of economic benefits will be required to settle the obligation; and
 - a reliable estimate can be made of the amount of the obligation.
- 223 Where it is unclear whether there is a present obligation, a past event is deemed to give rise to a present obligation if, taking account of all available evidence, it is more likely than not that a present obligation exists at the balance sheet date. For the purpose of this paragraph, the past event is the recognition in the financial statements of the premium by reference to which the levy is calculated. The declaration of a levy by the guarantee fund will clearly constitute sufficient evidence but, in addition consideration may need to be given to any statement of intent by the guarantee fund to raise further levies based on premium income already recognised in the financial statements, or any consistent trend in the amount and timing of levies in previous periods. Where the conditions for establishing a provision are not present, it will be necessary to consider whether the possibility of future levies should be disclosed in the notes to the financial statements as a contingent liability.
- 224 In relation to long term insurance business, it is appropriate to provide for levies related to future premium receipts (in respect of in-force business) within the long term business provision, unless those levies can be charged against assets held to cover linked liabilities.
- Profit and Loss Account
- 225 Where the amounts of general or long-term business are not material, the results should be disclosed as “other technical income, net of reinsurance” or “other technical charges, net of reinsurance” in the technical account for the business, which is material. Appropriate additional disclosure should be made in the notes to the financial statements in relation to the business accounted for in this way.
- 226 On consolidation, the result of any non-insurance entity belonging to the long-term fund may be included directly in the technical account for long-term business under item II.4 (Other technical income) or II.11 (Other technical charges) as appropriate. Where material, more detailed disclosure should be provided in the notes to the financial statements. Where an entity carrying on general insurance business is owned by the long-term fund, the result of this business should be transferred from the non-technical account to the technical account for long-term business using new lines for this purpose.
- 227 In the case of mutual insurance undertakings, no balance on the technical account for long-term business (item II.13) will normally arise as any surpluses or deficits on this account will be fully offset by transfers to or from the fund for future appropriations.
- 228 Paragraph 14 of FRS 3 requires that, where not shown on the face of the profit and loss account, an analysis between continuing operations, acquisitions (as a component of continuing operations) and discontinued operations of each of the other statutory profit and loss account format items between turnover and operating profit should be given by way of note. The analysis for insurance undertakings should only include the income and expenditure headings assigned with Arabic numerals in the profit and loss account format prescribed by Schedule 9A to the CA85 where the amounts concerned are material. More detailed information denoted by lower case letters in parenthesis need not be shown.

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FRS17 – Retirement
Benefits

- 229 For defined contribution schemes the contribution payable for the accounting period, and for defined benefit schemes the current service cost and any past service costs (including gains and losses on settlement and curtailments), should be included under the appropriate headings in the profit and loss account.
- 230 In relation to insurance business, the difference between the interest cost (ie the unwind of the discount on the pension liabilities) and the expected investment return on pension fund assets should be included as appropriate in the technical account for long-term insurance business or the non-technical account as a new line within Investment Income, or Investment Charges. These amounts should be disclosed separately in the notes to the financial statements.
- 231 Actuarial gains/losses, that is to say:
- Differences between the expected return on the scheme assets and the actual return;
 - the impact of experience variations on the scheme liabilities and the effect of changes in assumptions; and
 - adjustments because of limits on the amount that can be recognized as a pension fund asset in the balance sheet,
- should be disclosed in the Statement of Total Recognised Gains and Losses (STRGL) where these gains and losses are attributable to shareholders.
- 232 Any movement in actuarial gains or losses (as defined in paragraph **231**) which is not attributable to shareholders should be treated as an amount, the allocation of which either to policyholders or to shareholders has not been determined by the end of the financial year. It should be included as a separate line in the technical account for long-term insurance business immediately above the line for transfer to or from the fund for future appropriations, and reflected in that transfer. This is consistent with paragraph 27 of FRS3 (Reporting Financial Performance) which states that the components of the STRGL should be the gains and losses that are recognised in the period in so far as they are attributable to shareholders.
- 233 A pension asset or liability should be shown as the last item of the assets or liabilities section as appropriate. A subtotal of assets or liabilities should be disclosed immediately before the pension fund asset or liability.
- 234 Where the Fund for Future Appropriations is determined after taking account of a pension asset or a pension liability, the impact should be disclosed separately in the notes to the accounts.
- 235 The methodology adopted for calculating the longer term rate of investment return on pension scheme assets should be consistent with any method used for determining the longer term rate of return on investments held for the purpose of the insurance business.
- 236 In some group defined benefit schemes, it may not be possible for the individual companies in the group to identify their share of a pension asset or a pension liability. In these circumstances, individual group entities may account for the scheme as a defined contribution scheme but must in addition disclose:

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- (a) The fact that the scheme is a defined benefit scheme but that the employer is unable to identify its share of the underlying assets and liabilities; and
- (b) any available information about the existence of the surplus or deficit in the scheme and the implications of that surplus or deficit for the employer
- 237 However, in the consolidated accounts it will be necessary to account for the group scheme as a defined benefit scheme. The allocation of the defined benefit scheme surplus/deficit between that attributable to shareholders and that attributable to funds the allocation of which to policyholders or to shareholders has not been determined by the end of the financial year should reflect the extent to which each benefits (in the case of a surplus) or is disadvantaged (in the case of a deficit). Sufficient disclosure should be made to enable the accounting treatment to be understood.
- Estimation Techniques,
Uncertainty and
Contingent
Liabilities
- 238 The purpose of this section is to give guidance on the disclosure of uncertainties and estimation techniques required by FRS18 (Accounting policies). In addition, it introduces the requirement to give disclosure on contingent liabilities arising from insurance contracts in certain circumstances.
- 239 Uncertainties arising from insurance contracts can be classified for financial reporting purposes as follows:
- (a) General uncertainties arising where the range of outcomes for provisioning purposes is within a 'normal' range;
- (b) Specific uncertainties which are material and subject to an unusually wide range of outcomes;
- (c) Uncertainties in areas where FRS12 does not require a provision to be established but where that standard may require contingent liability disclosures.
- 240 There is inherent uncertainty in estimating many of the technical provisions in respect of liabilities arising from insurance business. Compliance with FRS 18 requires the following disclosures in the notes to the financial statements:
- A broad description of the factors giving rise to uncertainty;
 - A description of those items to which significant estimation techniques have been applied;
 - A description of the estimation techniques used;
 - Details of the significant assumptions made and information used in forming the estimates; and
 - A note of those factors to which the estimation technique is particularly sensitive.
- 241 Some disclosure relating to long-term business technical provisions is already required by paragraphs **184** to **187** of the SORP. These disclosures may need to be enhanced to include the matters referred to above.

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- 242 Where a specific material uncertainty results in the possibility of a range of outcomes outside the 'normal range', separate disclosure should be made. Disclosures should include the circumstances giving rise to this level of uncertainty, an indication of the uncertainties relating to the amount and timing of the outflows and the possibility of any related reimbursements.
- 243 Under FRS 18, estimates techniques are significant if the range of reasonable monetary outcomes is so large that the use of a different estimation technique could materially affect the view shown by the entity's financial statements. The description of a significant estimation technique will include details of those underlying assumptions to which the monetary amount is particularly sensitive.
- 244 FRS 18 also requires disclosure of the impact of significant changes to estimation techniques. Companies should consider those techniques and assumptions which have changed from year to year and where practicable make appropriate disclosure of the effect of significant changes in accordance with paragraph 55(d) of FRS 18.
- 245 Provisions, contingent liabilities and contingent assets arising from insurance contracts with policyholders are exempt from the requirements of FRS12 (Provisions, contingent liabilities and contingent assets). Notwithstanding this, however, insurers should apply the principles of paragraph 91 of FRS12 in certain circumstances.
- 246 Where provision has been made for liabilities and any contingency arises solely because those provisions are subject to a degree of uncertainty because estimation techniques have been used in their determination, the disclosure required by paragraph **238** to **242** above will be sufficient to alert users of financial statements to the fact that the amounts at which liabilities are settled may exceed the provisions recorded in the financial statements. In some cases, there will be considerable uncertainty concerning future events. In these circumstances, a degree of caution will be necessary in the exercise of the judgment required for setting provisions such that liabilities are not understated.
- 247 Where a specific material contingent liability arises in respect of an item for which no provision has been made in the financial statements, and the prospect of this resulting in a transfer of economic benefits is more than remote, the disclosure set out in paragraph 91 of FRS12 should be given. It should be noted that nothing in this paragraph should be read to suggest that a provision need not be made even where there is material uncertainty. As explained in paragraph 91 of FRS 12, the level of provision should be assessed having regard to the range of uncertainty as to the eventual outcome for the category of business in question.

Reporting the
Substance of
Reinsurance
Transactions –
General Principles

- 248 Paragraphs **250** to **255** and **258** to **261** below do not apply to rights and obligations under reinsurance contracts that do not satisfy the definition of an insurance contract in Appendix C of FRS 26, where FRS 26 has been adopted.
- 249 In accordance with FRS 5, the economic substance of a reinsurance transaction should be reflected in the result for the year and the balance sheet.

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- 250 A key characteristic of reinsurance is the transfer and assumption of significant insurance risk. There will be no transfer of insurance risk where the contract provides for the reinsurer to receive no more than a lender's rate of return under all reasonably possible scenarios. The assessment as to whether there has been a significant transfer of risk should be made having regard to the timing of all cash flows anticipated under the contract and any related contract.
- 251 The insurance risks relating to a long term reinsurance contract include mortality, morbidity, investment, persistency and expenses risks.
- 252 The insurance risks relating to a general reinsurance contract may consist of either or both of underwriting risk and timing risk.
- 253 In considering whether or not a significant transfer of insurance risk has taken place, the entity should consider first whether it is reasonably possible that the reinsurer may realise a significant loss from the contract and secondly whether there is reasonable possibility of a significant range of outcomes from the contract. Insurance risk will not have transferred unless both of these conditions exist. 'Significant' should be assessed in the context of the commercial substance of the contract or contracts being evaluated as a whole, and should be judged with reference to the range of outcomes that would reasonably be expected to occur in practice.
- 254 The assessment as to whether significant insurance risk is transferred should be made prospectively at the time the contract is entered into. The method of accounting should be followed consistently over the whole period of the contract. If there has been a material change in contract terms during the period of the contract, the entity should perform a new assessment of whether or not a significant transfer of insurance risk has occurred.
- 255 Any reinsurance contract should be accounted for in two parts where elements can be identified that do not result in the transfer of significant insurance risk.
- 256 A reinsurance contract can create new assets (eg a right to reinsurance recoveries) and liabilities (eg an obligation to pay premiums for the reinsurance) in the financial statements of the cedent. It cannot lead to assets and liabilities arising from the underlying reinsured business ceasing to be recognised.
- 257 To determine whether or not an asset and/or a liability has been created, a three stage process should be followed:
- consideration of the transaction in conjunction with any other where this is necessary to obtain an understanding of the overall commercial effect;
 - determination of the reasonably possible outcomes of the transaction having regard to its commercial effect, uncertainty and the intentions of the parties to the transaction insofar as these assist in determining its substance; and
 - assessment of whether assets and/or liabilities have been created based on the above stages.
- 258 Where a reinsurance contract covers more than one accounting period, the reinsured should remeasure future entitlements and liabilities under the contract at each balance sheet date. This remeasurement should have regard to experience under the contract

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		up to the balance sheet date and the amount, and for financial reinsurance the timing, of expected future cash flows.
	259	A provision should be made for any shortfall in value (eg any anticipated inability on the part of the reinsurer to meet its obligations to the cedent, when they are expected to fall due).
	260	Assets created by reinsurance transactions should normally be valued on the same basis as the related reinsured liabilities except in the circumstances covered in paragraph 259 .
	261	Where material, any financial reinsurance element should not result in a net credit to the profit and loss account at inception. The measurement of any asset created at inception through financial reinsurance should not exceed the corresponding liability to the reinsurer. To achieve this result an additional provision should be established. This provision should be released to the technical account for long-term or general insurance business on a systematic and rational basis over the period of the contract.
Presentation and Disclosure – Reinsurance Contracts	262	Reinsurance should be dealt with in the technical account for general business or the technical account for long-term business as appropriate provided the contract is one which may be accounted for as an reinsurance contract in accordance with paragraphs 250 to 255 . In accordance with FRS5, the economic substance of all reinsurance contracts must be reflected in the results for the year and the balance sheet. The presentation and disclosure of reinsurance contracts should be such as to enable a clear understanding of their effect on the results. Where or to the extent that, the application of FRS5 principles does not permit a reinsurance contract to be accounted for as insurance, the accounting treatment and disclosure should be appropriate to the nature of the contract.
	263	Reinsurance recoveries should be accounted for in the same accounting period as the related claim, and included in the balance sheet as an asset under Assets item Da3 (Reinsurers' share of technical provisions: claims outstanding). Although permitted under Schedule 9A to the CA85, the alternative method of showing reinsurance recoveries as a disclosed deduction from technical provisions is not permitted by the offset rule in FRS 5.
Reinsurance Balance	264	For the purpose of the disclosure required under paragraphs 75 and 76 of Part 1 of Schedule 9A to the CA85, the “ reinsurance balance ” means for general business the aggregate total of all those items included in the technical account for general business which relate to reinsurance outwards transactions including items recorded under item 1.7(d) (Reinsurance Commission and Profit Participations) and for long-term insurance business the corresponding items in the technical account for long-term business including items recorded under item 11.8(d) (Reinsurance Commissions and Profit Participations).

PART 6 - Accounting for Investments

FRS 26 (Financial Instruments: Measurement)	265	The guidance in this section applies in full to insurance undertakings that are not subject to the provisions of FRS 26 relating to financial assets. Where, and to the extent that an entity is subject to those provisions, paragraphs 266, 268 and 279-290 are not applicable.
Valuation of Investments Other than non-linked Land and buildings	266	Investments included under asset items CII, CIII and CIV should be stated in the balance sheet at their current value except for redeemable fixed income securities where the amortised cost basis of valuation has been adopted as permitted by paragraph 24 of Schedule 9A to the CA85. Assets held to cover linked liabilities should be stated in the balance sheet under assets item D at their current value at the balance sheet date. This paragraph and the provisions set out in paragraphs 285 – 298 do not apply to PVIF whether accounted for as an investment or otherwise.
Valuation of land and buildings excluding those held to cover linked liabilities	267	Land and buildings, excluding those held to cover linked liabilities, should be included under assets item CI. Investment properties as defined by SSAP19 should, in accordance with that Standard, be included in the balance sheet at their open market value and should not be subject to any periodic charge for depreciation. Self-occupied properties should be shown in the balance sheet at current value and, where material, a charge for depreciation should be made in accordance with FRS15. The book value of self-occupied properties included under assets item CI should be disclosed in the notes to the financial statements in accordance with Schedule 9A to the CA85.
Anticipated cost of realisation	268	Where, in accordance with paragraphs 25(4) and 26(6) of Part I of Schedule 9A to the CA85, the valuation takes into account the anticipated costs of realisation of investments subsequent to the balance sheet date, no allowance should be made for any reduction in the value of such investments subsequent to the balance sheet date.
Group companies	269	Shares in group undertakings (asset item CII.1) should be accounted for at current value in the parent company's individual balance sheet.
	270	In the consolidated financial statements, subject to paragraph 271 below, interests in group companies should be consolidated on a line by line basis as required by law, having regard also to paragraph 226 above.
	271	In the case of an interest in a group company belonging to the long term business fund, changes in the value of which affect or establish policyholders' rights, paragraph 3 (1A) of Schedule 4A to the CA85 prohibits any adjustment to the related insurance liabilities in the

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consolidated accounts. Where this necessitates the inclusion of an additional asset or liability in the balance sheet reflecting the difference between the current value and the net assets consolidated, the additional items should be included using a new line for this purpose.

Associates and Joint
Ventures

- 272 Interests in associates and joint ventures which form part of an investment portfolio within the meaning of paragraph 50 of FRS 9 should be accounted for as investments according to the method of accounting applied to other investments within the same portfolio rather than as associates or joint ventures. Other interests in associates and joint ventures should be accounted for in accordance with paragraphs **273** and **274**.
- 273 Interests in associates and joint ventures should be shown under asset item C.II.3 (Investments in group undertakings and participating interests: participating interests) in the parent company and consolidated financial statements. In the parent company's financial statements, they should be valued at current value.
- 274 In the consolidated financial statements, the equity or gross equity method of accounting should be adopted as required by FRS 9.
- 275 The provisions of paragraphs **271** will apply as appropriate to interests in associates and joint ventures.
- 276 The layout of the profit and loss account specified in Schedule 9A to the CA 85 is incompatible with the FRS 9 requirement to disclose the share of the operating results of associates and joint ventures immediately after group operating profit. Insurers should therefore comply with the FRS 9 disclosure requirement by including the amounts in the profit and loss account under Investment Income: income from participating interests (item 2(a) in the technical account for long-term insurance business and 3(a) in the non-technical account) and disclosing as a memorandum item in the non-technical account the amount of the group operating result attributable to the share of operating results of associates and joint ventures.
- 277 It is envisaged that insurers will not normally enter into joint arrangements that are not an entity. For this reason no guidance is given in this Statement on the appropriate accounting treatment. Insurers entering into this type of arrangement should follow the provisions of FRS 9.

Valuation
Movements

- 278 Movements in the value of interests in group companies, associates and joint ventures shown in the balance sheet at current value are not covered by the guidance on investment return set out in paragraphs **285** to **298**. Valuation movements on interests attributable to the long-term business (including the additional asset referred to in paragraph **271**) should be taken to the technical account for long-term business. Valuation movements on interests not attributable to the long-term business should be taken to revaluation reserve except where the interests form part of an investment portfolio in which case the valuation movements should be taken to the non-technical account.

Valuation at
Amortised cost

- 279 Use of the amortised cost basis of valuation is appropriate for redeemable fixed income securities which are part of a portfolio of such securities intended to be held on an ongoing basis in the activities of the insurance undertaking.

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- 280 The amortised cost basis of valuation is inappropriate for irredeemable fixed interest stocks and accordingly these should be accounted for at current value.
- 281 Where redeemable fixed income securities are valued at amortised cost, any excess of the purchase price over the amount repayable at maturity should be charged to the profit and loss account by instalments so that it is completely written off when the securities are redeemed. Any excess of maturity value over purchase price should be released to profit and loss account by instalments over the period remaining until repayment.
- 282 Where, in relation to a security which has been valued at amortised cost, there is a choice of redemption dates, and the amortised cost should be computed on the basis of the redemption date, which would give the lowest yield measured from the date of purchase.
- 283 The amortised cost should be reduced if necessary to take account of any permanent diminution in value arising from potential default losses.
- 284 In respect of investments valued at amortised cost the following disclosures should be made, analysed between investments attributable to the long term business and other investments:
- the aggregate totals of the purchase price, the amortised cost and current value; and
 - the net excess/deficit of the amounts payable at maturity over the amortised cost.
- Accounting
Treatment of
Investment Return
- 285 Whilst insurance companies have the option under Schedule 9A to take unrealised **investment gains and losses** to revaluation reserve (and the statement of total recognised gains and losses), the distinction between realised and unrealised gains and losses on readily marketable investments is largely irrelevant. Accordingly, (subject to paragraph **278** above) all such realised and unrealised gains and losses should be taken to the profit and loss account.
- 286 In accordance with Notes 8 and 9 to the profit and loss account format in Part I of Schedule 9A to the CA 85, the **investment return** arising during the accounting period in relation to investments which are directly connected with the carrying on of long term insurance business should initially be included in the technical account for long term business. These investments comprise those arising in, or attributed to, the long-term fund including the fund for future appropriations together with such directly connected investments where the return accrues to shareholders whether held within or outside the long-term business fund.
- 287 The investment return arising in relation to all other investments including realised and unrealised investment gains and losses should initially be taken to the non-technical account.
- 288 Amortisation amounts, which are charged or released to the profit and loss account in accordance with paragraph **281** above should be disclosed as investment income in item III.3 (b)(bb) of the non-technical account (Income from other investments) or item II.2 (b)(bb) of the long-term business technical account (Income from other investments) as appropriate.

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	289	Where redeemable fixed income securities valued in the balance sheet at amortised cost are disposed of, the difference between the net sale proceeds and carrying value should be recognised in full in the profit and loss account of the period in which the disposal takes place. This is notwithstanding that the proceeds may be used to purchase other debt securities and fixed income securities which are also valued at amortised cost.
	290	However, for the purpose of calculating the longer term rate of investment return, it may be appropriate to spread these realised gains or losses over the period to maturity (or deemed maturity) of the investments sold. (See paragraph 303).
Allocation of Investment Return	291	In assessing the performance and financial position of their operations, insurers will usually consider the longer term investment performance to be more important than the investment return arising in the accounting period. Therefore, this SORP permits, but does not require, a form of presentation which enables the reader to identify operating results based on the longer term rate of investment return. This return may be recorded within the general business and long-term business technical accounts and may also be disclosed separately as part of the total operating profit.
	292	Where investment return is allocated, it should be on one of the following bases: <ul style="list-style-type: none">• The longer term rate of return basis (see paragraphs 295 to 298); or• an allocation of the actual investment return on investments supporting the general insurance technical provisions and associated shareholders' funds should be made from the non-technical account to the technical account for general business.
	293	To ensure consistency of treatment in the case of an insurance company or group transacting both general and long term insurance business: <ul style="list-style-type: none">• where the longer term rate basis of allocation is used, it must be applied to both the general and long term insurance business; and• where an allocation of the actual investment return on investments supporting the general business technical provisions and associated shareholders' funds is made from the non-technical account to the technical account for general business, no allocation of investment return should be made from the technical account for long term business to the non-technical account.
	294	The reasons for making allocations of investment return within the profit and loss account and the bases on which they are made should be disclosed in the notes to the accounts.
Longer Term Rate Allocation Basis	295	The allocation of investment return from item II.12 (Allocated investment return transferred to the non-technical account) of the technical account for long-term business to item III.4 (Allocated investment return transferred from the long term business technical account) of the non-technical account should be such that the investment return remaining in the technical account for long term business on investments directly attributable to shareholders reflects

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the longer term rate of return on these investments. For this purpose, the investments directly attributable to shareholders are those supporting the long-term business other than assets supporting

- (i) the long term business provision,
- (ii) the fund for future appropriations; and
- (iii) the technical provision for linked liabilities.

- 296 The allocation from item III.6 (Allocated investment return transferred to the general business technical account) of the non-technical account to item I.2 (Allocated investment return transferred from the non-technical account) of the technical account for general business should be based on the longer term rate of investment return on investments supporting the general insurance technical provisions and all the relevant shareholders' funds. The technical account for general business will then include the longer-term investment return relating to the investments attributable to the general insurance business.
- 297 Where it is necessary for the purpose of reflecting the longer term rate of investment return in the technical account for general business, the allocation referred to in paragraph 296 above may exceed the actual investment return of the accounting period on the corresponding investments. Similarly, the allocation referred to in paragraph 295 above may be of a negative amount which increases rather than decreases the amount of investment return included in the long term business technical account.
- 298 The allocation referred to in paragraph 295 above should be included in line II.12 of the long-term business technical account and in item III.4 of the non-technical account gross of any attributable tax. The tax attributable to the allocated investment return should be deducted from the tax attributable to long-term business in item II.11a of the long term business technical account and added to the tax on profit or loss on ordinary activities in item III.9 of the non-technical account.

The Longer Term Rate of Investment Return

Equities and
Properties

- 299 The longer term investment return on equities and properties should be determined using one of the following methods:
- grossing-up actual income earned for each asset class by a factor representing the longer term rate of investment return divided by an assumed long term dividend or rental yield (based on the assumption that income will reflect the mix of assets held during the accounting period). Adjustments will be required for special factors which may distort the underlying yields of the portfolio such as (in the case of equities), special or stock dividends and share buy-backs; or
 - Applying the longer term rate of return to investible assets held during the period (taking account of new money invested and changes in portfolio mix) by reference to the quarterly or monthly weighted average of each group of assets after excluding the effect of short term market movements.

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	300	The longer-term rate of return should be determined separately for equities and property and for each material currency in which relevant investments are held.
	301	<p>Taking into account the investment policy followed by the undertaking, the longer-term rate of investment return should reflect a combination of historical experience and current market expectations for each geographical area and each category of investments. The rates chosen should be best estimates based on historical market real rates of return and current inflation expectations, having regard, where appropriate, to the following factors:</p> <ul style="list-style-type: none">• comparison of the business's actual returns and market returns over the previous five years or such longer period as may be appropriate;• Longer-term rates of return currently used in the business for other purposes, for example, product pricing, with profits bonus policy, and pensions funding;• the rate used for the purpose of achieved profits method reporting;• consensus economic and investment market forecasts of investment returns; and• any political and economic factors which may influence current returns.
	302	Rates of return should be set with a view to ensuring that longer-term returns credited to operating results do not consistently exceed or fall below actual returns being earned. Any downturn in expectations of longer-term returns should be recognised immediately by reducing the assumed rate of return. Rates used should be reviewed at least annually although changes would be expected to be infrequent.
Fixed Income Securities	303	In the case of redeemable fixed income securities, the longer term rate of return may be determined by using either a redemption yield calculated on principles similar to that defined in paragraph 281 or the amortised cost basis with realised gains and losses subject to continuing amortisation over the remaining period to the maturity date. However, it may be based on interest earned where the net effect of amortisation would be immaterial. In the case of irredeemable fixed interest securities and short-term assets, the allocated longer-term rate of investment return should be the interest income receivable in respect of the financial year.
Derivatives	304	Where derivatives have a material effect and are used to adjust exposure to the various classes of investments, the calculation of the longer term rate of return set out in paragraphs 299 to 302 should be adjusted to reflect the underlying economic exposure.
Disclosure	305	<p>Where technical results are disclosed which reflect the longer term rate of investment return the following disclosures should be made in the notes to the financial statements:</p> <ul style="list-style-type: none">• The methodology used to determine the longer-term rate of return for each investment category;

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		<ul style="list-style-type: none"> • For each investment category and material currency, both the longer term rates of return and, if applicable, the long term dividend and rental yields used to calculate the grossing-up factor for equities and property; • A comparison over a longer term (at least five years) of the actual return achieved with the return allocated using the longer term rate of return analysed between returns relating to general business, long term business and other; and • The sensitivity of the longer-term investment return to a 1% decrease and a 1% increase in the longer-term rate of investment return.
Disclosure of Total Operating Profit	306	<p>Where technical results are determined taking into account longer term levels of investment return, supplementary disclosure may be provided by way of a memorandum item in the non-technical account of:</p> <ul style="list-style-type: none"> • the operating profit based on the longer term level of investment return; and • the difference between the actual and longer term levels of investment return arising in the accounting period as a result of short term fluctuations in investment return. <p>307 An alternative earnings per share figure reflecting the result based on the longer term rate of investment return may also be shown.</p>
Segmental Reporting	308	<p>Where allocations of investment return are made, the profit before tax of each segment shown in the segmental analysis should be based on the longer-term investment returns. The segmental results should be reconciled to the total of the actual result before tax disclosed in the non-technical account.</p>
Aggregation of Investment Gains/Losses	309	<p>The headings for realised and unrealised investment gains/losses in the profit and loss account should include the overall gains net of losses or losses net of gains as a single figure. It is not necessary to disclose separately the aggregate investment gains and aggregate investment losses.</p>
Investment Income	310	<p>Rents and interest income should be recognised on an accruals basis. Dividends receivable should be recognised in the financial statements on the date on which the price of the investment is quoted "ex-dividend".</p>
Investments in Unit Trusts/Open Ended Investment Companies (OEICs)	311	<p>Except for investments held to cover linked liabilities shown under assets item D, all investments in unit trusts and OEICs should be included in the balance sheet under assets item CIII.1 (Shares and other variable yield securities and units in unit trusts) regardless of the nature of the underlying assets of the unit trusts.</p>
FRS 25	312	<p>The presentation requirements of FRS 25 (Financial Instruments: Disclosure and Presentation) will apply with effect from accounting periods beginning on or after 1 January 2005. Financial instruments that are rights and obligations under an insurance contract as defined in Appendix C of FRS 26 are outside the scope of FRS 25.</p>

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The disclosure requirements of FRS 25 will apply insofar as entities are subject to FRS 26 with effect from no later than the accounting period in which FRS 26 is given effect by the entity.

PART 8 - Effective Date

- 313 This statement, which replaces the statement issued in November 2003 applies to financial statements for accounting periods beginning on or after 1 January 2005. In accordance with paragraph 58 of FRS 18 (Accounting Policies), entities should state in relation to their financial statements commencing in 2005 whether they have complied with this statement .

PART 9 - Legal Requirements

- Great Britain 314 The provisions of the EU Insurance Accounts Directive have been implemented in Great Britain by the Companies Act 1985 (Insurance Companies Accounts) Regulations 1993 and, for insurance undertakings not formed and registered under the CA85, by the Insurance Accounts Directive (Miscellaneous Insurance Undertakings) Regulations 1993.
- 315 Under these regulations, the old Schedule 9A to the CA85 was replaced by a new Schedule 9A. In consequence, the disclosure exemptions available to insurers in the old Schedule 9A have been withdrawn. Moreover, the financial statements of insurance undertakings are now required to show a true and fair view. The references in this Part are to the new Schedule 9A.
- 316 Insurance undertakings have been required to comply with the new Schedule 9A to the CA85 in financial statements for financial years commencing on or after 23 December 1994.
- Chapter I of Part I 317 Section A lays down general rules on the layout of insurers' financial statements and the extent to which items appearing under separate headings may be combined in the accounts, although separate disclosure may be required in the notes. In particular, paragraph 4 provides that, subject to the provisions of Schedule 9A, amounts in respect of items representing assets or income may not be set off against amounts in respect of items representing liabilities or expenditure (as the case may be) or vice versa.
- 318 Section B lays down required formats for the balance sheet and profit and loss account of an insurance undertaking. The notes to the accounting formats define certain items appearing in the financial statements and in some cases prescribe the accounting treatment to be applied. In particular Note 17 to the balance sheet format includes provisions governing the accounting treatment of deferred acquisition costs and Note 19 defines the fund for future appropriations. The long-term business provision is defined in Note 21 and the technical provision for linked liabilities is defined in Note 26. Acquisition costs and administrative expenses are defined in Notes 6 and 7 to the profit and loss account formats respectively. Notes 8 and 9 prescribe the accounting treatment of investment income, expenses and charges, and unrealised gains and losses on investments. Note 10 permits certain allocations of investment return to be made between the technical and non-technical accounts.
- 319 Paragraph 10 requires every balance sheet of a company which carries on long term business to show separately as an additional item the aggregate of any amounts included in balance sheet liabilities item A (capital and reserves) which are required not to be treated as realised profits under Section 268 of the CA85. A company which carries on long term business shall show separately, in the balance sheet or in the notes to the accounts, the total amount of assets representing the long term fund valued in accordance with the provision of Schedule 9A to the CA85.
- Chapter II of Part I 320 Section A lays down general accounting principles in relation to insurers' financial statements. In particular, paragraph 15 requires accounting policies to be applied consistently within the same

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accounts and from one financial year to another. Paragraph 19 provides that, if it appears to the directors that there are special reasons for departing from any of the principles stated in Section A in preparing the company's accounts in respect of any financial year they may do so, but particulars of the departure, the reasons for it and its effect shall be given in a note to the accounts.

- 321 Section B lays down current value accounting rules for assets. In particular paragraph 22 requires investments included under assets items C and D in the required balance sheet format to be disclosed in the balance sheet at current value. Paragraph 28 requires the purchase price of these investments to be disclosed in the notes to the accounts.
- 322 Paragraphs 25 and 26 lay down requirements for determining respectively the current value of investments (other than land and buildings) and land and buildings.
- 323 Paragraph 24 permits debt securities and other fixed income securities shown as assets under Assets item CII (investments in group undertakings and participating interests) and CIII (other financial investments) to be included in the balance sheet at amortised cost. Both the purchase price and current value of securities valued at amortised cost in the balance sheet must be disclosed in the notes to the accounts.
- 324 Paragraph 32 in Section C requires assets included under Assets item CI (land and buildings) to be depreciated but paragraph 27 in Section B provides that in this case the depreciation is to be calculated by reference to the most recently determined current value. Paragraph 10 of SSAP 19 (accounting for investment properties) provides however that investment properties should not be subject to periodic charges for depreciation except for properties held on lease which should be depreciated on the basis set out in FRS 15 at least over the period when the unexpired term is 20 years or less.
- 325 Section D lays down rules for determining insurance technical provisions. Paragraph 43 sets out the general requirement for the amounts of technical provisions and paragraphs 46 and 47 contain rules governing respectively the computation of the long-term business provision, and general business outstanding claims. Paragraph 47(7) prohibits implicit discounting of claims provisions in relation to general business. Paragraph 48 permits explicit discounting of general business claims provisions subject to certain conditions being satisfied while paragraphs 51-53 describe the two methods permitted for accounting on a non-annual basis.

Chapter III of Part I
Of Schedule 9A

- 326 This sets out the information which insurance undertakings are required to include in the notes to their accounts. Paragraphs 75-78, however, apply only to individual insurance undertakings and the information, which they require, need not be given in the financial statements of insurance groups, which do not include entity profit and loss accounts.

Chapter IV of Part I
Of Schedule 9A

- 327 Paragraph 81 includes certain definitions of terms referred to in the Schedule 9A. In particular, the "long term fund" is defined as the fund or funds maintained by a company in respect of its long term business in accordance with the provisions of the Insurance Companies Act 1982.

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Part II of Schedule
9A

- 328 This provides for the application of Schedule 4A to the CA85 to insurance groups with certain modifications. In particular, consolidated accounts of insurance groups must comply so far as practicable with the provisions of Part I of Schedule 9A as if the undertakings included in the consolidation were a single company.
- 329 For this purpose, section 255A(5) of the CA85 defines an insurance group as one where the parent company is an insurance company or where:
- (a) the parent company's principal subsidiary undertakings are wholly or mainly insurance companies, and
 - (b) the parent company does not itself carry on any material business apart from the acquisition, management and disposal of interests in subsidiary undertakings.
- 330 Paragraph 1(4) provides that sub-paragraph (1) of paragraph 3 of Schedule 4A to the CA85 shall not apply to those liabilities items the valuation of which by the undertakings included in a consolidation is based on the application of provisions applying only to insurance undertakings, nor to those assets items changes in the values of which also affect or establish policyholder's rights.
- 331 Paragraph 1(5) provides that sub-paragraphs (1) and (2) of paragraph 6 of Schedule 4A to the CA85 need not be complied with:
- (i) where a transaction has been concluded according to normal market conditions and a policyholder has rights in respect of that transaction, or
 - (ii) if the amounts concerned are not material for the purpose of giving a true and fair view.
- Northern Ireland 332 The Insurance Accounts Directive is implemented in Northern Ireland by the Companies (1986 Order) (Insurance Companies Accounts) Regulations 1994.
- Recent
EU Legislation 333 For each financial year starting on or after 1 January 2005, Regulation (EC) No 1606/2002 of the European Parliament and of the Council requires the consolidated accounts of publicly traded companies to be prepared in conformity with such IAS as have been endorsed by the EU Commission for application in Europe. Member states may permit or require a listed parent company and unlisted groups and companies to prepare their financial statements in accordance with such IAS.
- 334 The Companies Act 1985 (International Accounting Standards and Other Accounting Amendments) Regulations 2004 amend the CA 85 to permit but not require listed parent companies and unlisted groups and companies to prepare their financial statements in accordance with EU endorsed IAS. Section 227C(1) of the CA 85 as amended requires the directors of a parent company to secure that the individual accounts of (a) the parent company and (b) each of its subsidiary undertakings falling within the scope of the Act are all prepared using the same financial reporting framework, except to the extent that in their opinion there are good reasons for not doing so. However, where the directors of a parent company prepare IAS group accounts, section 227C(5) permits the individual accounts of the parent company to be prepared under IAS, and the requirement of section 227C(1) then only applies to each of the subsidiaries falling within the scope of the CA85.

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- 335 The Regulations also insert a new Section BA into Schedule 9A of the CA85 to implement the provisions of the EU “Fair Value Directive” (2001/65/EEC). This provides inter alia that certain financial instruments (including derivatives) may be included in the financial statements at fair value.