abbey

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Dear Peter

Comments on ED 5 Insurance Contracts (Phase I)

Abbey is a member of the British Bankers Association ("BBA") and has participated in the preparation of, and supports, its response dated 30 October 2003. The BBA response contains answers to the specific questions raised in the exposure draft.

Overall we remain concerned that there is insufficient time for the Phase 1 standard to be finalised in time for 2005 implementation to be practical. Greater consideration should therefore be given to retaining the use of existing local GAAP for all insurance contracts until the Phase 2 project is finalised. This would include all those contracts, which ED5 proposes should be accounted for under IAS39. This would allow the significant issues that remain with the current two-phased approach to be resolved.

If however, the decision is taken to proceed with the proposed split between insurance and investment contracts, then there are a number of areas where clarification is required if the split is to be implemented on a consistent basis across insurance companies. Examples of areas where our initial implementation work has highlighted these types of issues are highlighted below.

a) Measurement of insurance risk
Clarity is required in relation to a wide range of specific product classification issues:

- The appropriateness of using a comparison of death benefits to surrender values to determine whether insurance risk is significant;
- Market value adjustments;
- Temporary surrender penalties;
- Investment contracts with additional life cover options;
- Products offering a choice of funds in which to invest, each fund carrying different levels of insurance risk — we assume that if there is any possibility of the contracts becoming insurance contracts over their life because the insurance risk becomes significant, they should always be treated as insurance rather than investment contracts, but this should be confirmed;
- Initial and ordinary units within one contract type (initial units carrying surrender penalties whilst ordinary units do not).

b) Level at which insurance risk will be deemed 'significant'
Based on a comparison of surrender values to death benefits, guidance is required as to what percentage difference should be deemed 'significant' In the absence of a specific percentage test, detailed guidance, including worked examples, is required to attempt to avoid different assumptions being used across the industry.

c) Fair value of insurance assets and liabilities
Fair value insurance assets and liabilities are required for 31 December 2006, although comparatives are not required until 2007. These implementation dates are likely to be unrealistic given that no detailed guidance currently exists on how to fair value insurance assets and liabilities.

d) ED 5 and IAS 27
Currently our Group accounts reflect an embedded value profit figure in respect of our insurance companies. For comparative purposes in 2005, this presents an issue in that IAS 27 requires retrospective application resulting in a line by line consolidated position, whereas our comparative figure in respect of our insurance and investment products will be an embedded value profit figure. Detailed implementation guidance is required to avoid significant confusion, particularly for readers of the accounts.

e) Deposit accounting
Clarity is sought as to whether the IAS 39 measurement exemption in respect of discretionary participation features applies also to the presentation of premiums received and accounted for as a deposit.

I hope you find these comments helpful and that you will be able to take them into account.

Yours sincerely

Ken Luscombe

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Abbey