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Your ref.
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Date 31 OCT 03

Dear Mr. Clarke

ED5 INSURANCE CONTRACTS

Please find below Co-operative Insurance Society Limited (CIS) response to the questions listed within the Exposure Draft 5 'Insurance Contracts' that are considered to have a more significant impact on the accounting and business environment of CIS.

Our principal concern is around the wider reporting environment for insurers. Considerable uncertainty remains over the final shape of Reporting Standards and disclosure requirements and very substantial gaps in guidance will remain during the period in which insurers must address compliance with International Financial Reporting Standards and beyond. Indeed, the proposal under ED5 is in itself a stop-gap solution to accounting for insurance contracts in preparation for Phase II of a Standard, which proposes a measurement and recognition basis on an asset/liability model.

Question 4 – Temporary exclusion from criteria in IAS 8

(a) Paragraphs 5 and 6 of [the May 2002 Exposure Draft of improvements to] IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* specify criteria for an entity to use in developing an accounting policy for an item if no IFRS applies specifically to that item. However, for accounting periods beginning before 1 January 2007, the proposals in the draft IFRS on insurance contracts would exempt an insurer from applying those criteria to most aspects of its existing accounting policies for:

(i) insurance contracts (including reinsurance contracts) that it issues; and

(ii) reinsurance contracts that it holds.

(paragraph 9 of the draft IFRS and paragraphs BC52-BC58 of the Basis for Conclusions).

Is it appropriate to grant this exemption from the criteria in paragraphs 5 and 6 of [draft] IAS 8? If not, what changes would you suggest and why?

(b) Despite the temporary exemption from the criteria in [draft] IAS 8, the proposals in paragraphs 10-13 of the draft IFRS would:

(i) eliminate catastrophe and equalisation provisions.

(ii) **require a loss recognition test if no such test exists under an insurer's existing accounting policies.**

(iii) **require an insurer to keep insurance liabilities in its balance sheet until they are discharged or cancelled, or expire, and to report insurance liabilities without offsetting them against related reinsurance assets (paragraphs 10-13 of the draft IFRS and paragraphs BC58-BC75 of the Basis for Conclusions).**

Are these proposals appropriate? If not, what changes would you propose, and why?

<u>CIS response</u>

(a) The proposed exemption to the criteria specified within IAS 8 is appropriate given that an International Financial Reporting Standard (IFRS) will not be available for the recognition and measurement of Insurance Contracts prior to the application of International Accounting Standards to financial statements for year-ends 2005 onwards.

However we consider that limiting the exemption to accounting periods prior to 1 January 2007 is unreasonable given the current status and potential issues surrounding the introduction of such an IFRS. We therefore feel that the exemption should remain in force until an IFRS is published and applicable.

(b) (i) We consider the elimination of catastrophe and equalisation provisions to be an appropriate accounting treatment. However, it is unreasonable given the current UK statutory requirement for recognition to remove these provisions until local jurisdictions have agreed to relax such requirements.

(ii) We agree that a loss recognition test is appropriate and is consistent with current UK accounting methodology. However, further guidance should be provided within the Standard to indicate at what level the loss recognition test should be applied e.g. policy, class or business level.

(iii) We agree that the requirement to keep insurance liabilities in the balance sheet until they are discharged, cancelled or expired is appropriate. Likewise, we are in agreement that insurance assets and liabilities should not be offset.

Question 10 – Disclosure of the fair value of insurance assets and insurance liabilities

The proposals would require an insurer to disclose the fair value of its insurance assets and insurance liabilities from 31 December 2006 (paragraphs 30 and 33 of the draft IFRS, paragraphs BC138-BC140 of the Basis for Conclusions and paragraphs IG60 and IG61 of the draft Implementation Guidance).

Is it appropriate to require this disclosure? If so, when should it be required for the first time? If not, what changes would you suggest and why?

<u>CIS response</u>

We consider that, currently, this is an unreasonable requirement given the lack of guidance available on the measurement of insurance assets and liabilities on a fair value basis. The proposed 'phase II' of the exposure draft is not expected until late 2004, which allowing for a period for comment, may result in a much-delayed Standard.

We also believe that the requirement for disclosure without adequate guidance will lead to a lack of comparability between various insurance entities depending on the valuation technique employed in the interim. We therefore question the value of such disclosures of fair values until detailed guidance is available. Furthermore, quantification of such disclosures will necessitate entities incurring significant costs on new valuation systems, with the risk that further costs are incurred in the event that interim valuation bases are inconsistent with the ultimate fair value model.

For the reasons given above we consider that this requirement should be removed from the Standard and be included in the remit of ‘phase II’ of the Insurance Contracts Standard.

Question 13 – Other comments

Do you have any other comments on the draft IFRS and draft Implementation Guidance?

CIS response

(a) Current status of certain Standards applicable to Insurance entities

We have a general concern on the current status of IAS / IFRS that will be applicable to insurance entities, namely ED5, IAS 32 and IAS 39 for accounting periods ending 2005.

Both of the current Financial Instrument Standards will have a significant impact to CIS in terms of financial investments and ‘investment contracts’ but are in the process of undergoing amendment. We recognise that the IASB is proposing exemptions from applying these Standards for 2004 comparatives and welcome such exemptions given the Standards’ status. However, the appropriate solution is to revise the Standards as soon as possible.

(b) Disclosure requirements

We recognise that the IASB objective is to add value and aid understanding to the users of accounts by proposing a more extensive disclosure both for insurance contracts and financial instruments under IAS 32. However we are concerned that the current requirements could result in a significant degree of subjectivity leading to a lack of comparability between entities as well as placing an unnecessarily onerous burden on entities to generate very extensive disclosures. We urge the development of more concise disclosure framework, including more prescriptive guidance on key disclosures.

Yours sincerely,

D. Grattan
Finance Executive, Director