



By email to: ukfrs@frc.org.uk

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10 February 2016

Dear Madam

FRED 64 - Draft amendments to FRS 103 – Insurance Contracts – Solvency II

PricewaterhouseCoopers LLP welcome the opportunity to comment on the proposed amendments to FRS 103. Our responses to the questions asked by the FRC and other comments are given below. In particular we welcome the FRC's efforts to keep the wording of FRS 103 updated to reflect changes in regulation and we agree that any amendments should allow insurers who are existing reporters to continue applying their established accounting policies should they wish to do so. However, as discussed in our response to question 2, we do not agree that insurers applying FRS 103 for the first time (referred to in this response as 'new entrants') should be required to assess their accounting policies against a 'benchmark' which is a now obsolete regulatory regime.

Question 1

Do you agree with the amendments proposed to FRS 103 and the related Implementation Guidance? If not, why not?

Comments:

We agree that FRS 103 should be updated to reflect changes in regulation and we agree that any amendments should allow insurers who are existing reporters to continue applying their established accounting policies should they wish to do so. However, as discussed below, we have some concerns regarding the approach proposed to achieve these aims.

It is proposed that references to the PRA's rules are removed from the definition of 'realistic value of liabilities' with the interpretation of the term required to 'be consistent with that applied in periods ending before 1 January 2016'. The same approach is proposed to what was previously 'the modified statutory solvency basis' (MSSB) which has now been renamed as the 'established long-term insurance business liability basis'. It is proposed that the definition of 'statutory solvency basis' be deleted.

The definition of the realistic value of liabilities now includes some terms which require further guidance in order to be able to be consistently applied (i.e. 'with-profits benefits reserve; 'future policy related liabilities'; and 'realistic current liabilities'). The definition of the 'established long-term insurance business liability' is based on high level principles (e.g. appropriateness) which require

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further guidance in order to be consistently applied. The requirement for the interpretation of these terms to be 'consistent with that applied in periods ending before 1 January 2016' provides some guidance for existing reporters; however there is no such clarification for new entrants. We therefore do not believe these revised definitions are the most appropriate.

Given that the intention is that the interpretation of these terms should be unchanged, we would suggest that the definitions of MSSB, the 'statutory solvency basis' and 'realistic value of liabilities' also remain unchanged save that references to INSPRU are amended to be references to 'INSPRU as at 31 December 2015'.

Further drafting comments are set out in the Appendix to this letter.

Question 2

Have you identified any other amendments that you consider should be made to FRS 103 or the related Implementation Guidance as a result of the changes in the regulatory framework? If so, please provide details of your proposed amendments and the rationale for them.

Comments:

Yes. Following the proposed changes we do not believe that Section 3 of FRS 103 provides an appropriate benchmark against which new entrants should assess their accounting policies.

As set out in paragraph 1.5 of FRS 103, "Entities that are setting accounting policies ... for the first time, shall first consider the requirements of Section 3 ... as a means of establishing current practice as a benchmark before assessing whether to set accounting policies that differ from those benchmark policies...".

The amendments being proposed to Section 3 seek, in substance, to preserve the accounting treatment that was previously described as the 'realistic capital regime' as this benchmark whilst no longer referring to PRA's rules (see response to question 1). This represents the basis of regulatory accounting that UK insurers were required to apply until 31 December 2015 but which is no longer applicable to insurers that are subject to Solvency II. As such it does not represent 'current practice' as referred to in paragraph 1.5 of FRS 103.

Section 3 currently imposes no practical constraints on existing reporters as, under paragraph 3.2, they do not have to comply with it if they change their accounting policies in accordance with paragraph 2.3 of FRS 103. As a result consideration of the ongoing relevance of Section 3 should most appropriately focus on whether it continues to provide an appropriate benchmark for new entrants.

In our view an obsolete regulatory regime (for insurers within the scope of Solvency II) is not an appropriate benchmark for new entrants to use in 'assessing whether to set accounting policies that differ from those benchmark policies'. In particular:

- Policies based on an obsolete regulatory regime do not represent current practice and consequently do not constitute a relevant benchmark against which to assess accounting policies.



- It may be unduly burdensome to require new entrants to assess their proposed accounting policies against a benchmark that they would not have to consider for regulatory (or any other) purposes.

It is recognised that it may be impractical for the FRC to develop a new, more relevant and less burdensome, benchmark against which new entrants would assess their accounting policies. As a result we propose the deletion of Section 3 of FRS 103. Whilst this would mean that there was now no explicit benchmark against which new entrants are required to assess their accounting policies we note that this would be consistent with the position applicable to insurers reporting under both full IFRS and FRS 101. Such a deletion would not have a practical impact on existing reporters.

To the extent that the content of Section 3 is relevant to those insurers that apply accounting policies based on (what was previously referred to as) the realistic capital regime or the MSSB, then its content could be incorporated into the non-mandatory implementation guidance to FRS 103.

Please contact Mike Vickery via mike.p.vickery@uk.pwc.com if you would like to discuss the contents of this letter.

Yours faithfully

PricewaterhouseCoopers LLP



Appendix – Further drafting comments

1. We suggest the sentence “The detailed methodology for UK companies is included in regulations contained in the PRA Rulebook” be deleted from the definition of 'net premium method' as insurers within the scope of Solvency II will not be subject to the regulations referred to.
2. We suggest that the definition of ‘with-profits business’ should no longer make reference to the ‘long-term fund’, given that the concept of the long-term fund is disapplied for Solvency II insurers from 1 January 2016. Consistent with the PRA Rulebook Glossary definition of ‘with-profits policy’ the term ‘with-profits business’ could instead be defined to mean ‘Long-term insurance business which provides benefits through eligibility to participate in discretionary distributions based on profits arising from the insurer’s business or from a particular part of the insurer’s business’.
3. We suggest amending the first sentence of IG1.7 to read “Paragraph 3.12 of FRS 103 permits the recognition of a VIF asset where the determination of the realistic value of liabilities takes account of this value” in order to more accurately reflect the requirements of paragraph 3.12.