LIBA

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31 October 2003

Peter Clark
Senior Project Manager
International Accounting Standards Board
30 Cannon Street
London
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By email to: CommentLetters@iasb.org.uk

Dear Mr Clark,

Exposure Draft ED 5 Insurance Contracts

I am writing on behalf of LIBA (the London Investment Banking Association) to comment on the above Exposure Draft. LIBA is, as you may know, the principal UK trade association for investment banks and securities houses; a full list of our members is attached.

In studying the proposals set out in the Exposure Draft, we have focused particularly on those areas where there may be implications for accounting in the financial sectors in which our members principally operate. Overall, we support the approach taken in the ED, but we have identified a number of points which we believe the Board should consider. Our comments, which are set out below, follow the structure of the Questions in the "Invitation to Comment" section of the Exposure Draft; please note that we have not answered every question.

Question 1 – Scope

We agree with the proposed scope of the IFRS. In particular, we support the proposal that weather derivatives should be considered to be financial instruments and should therefore be brought within the scope of IAS 39.

Where contracts fall within IAS 39, we do not believe it is either appropriate or helpful for further guidance on the accounting for such instruments to be included in this IFRS. For example, we believe paragraph B19 would be more helpful if it merely provided a direct cross-reference to the guidance in IAS 39.

Question 2 – Definition of Insurance Contract

We are generally comfortable with the proposed definition of an insurance contract, and particularly with the various examples of contracts given in paragraphs B17 and B18. However, we are concerned that the application of all the defined terms in Appendix A may not always result in an appropriate analysis of contracts. In particular, the inclusion of 'other variable' in the definition of 'financial risk' could give rise to ambiguity: we believe it would be better to reverse the existing approach to defining risk by providing an explicit definition of 'insurance risk' and to make 'financial risk' the default.

Question 5 – Changes in Accounting Policies

We support the proposal to restrict changes in accounting policies for insurance contracts where such a change would move an organisation away from the long term objective of fair value accounting for insurance contracts. We have however identified an issue for those companies that may start to enter into insurance contracts before Phase II of the insurance accounting project is completed:

- While it is clear that the future treatment of insurance contracts is moving towards the full use of fair value, there is no indication that such an approach is considered appropriate for those entities required to account for insurance contracts for the first time. Paragraph BC 6(b) includes in the Board's tentative conclusions for Phase II (as at January 2003) the statement that (subject to certain caveats) "assets and liabilities arising from insurance contracts should be measured at their fair value".

- Neither the proposed IFRS, nor IAS 1, nor the proposed revised IAS 8 (as included in the May 2002 Improvements ED), indicate that an entity accounting for insurance contracts for the first time would be able to measure them at fair value from the outset. The position for entities changing their accounting policies is clear, in that they should not move away from an approach which provides a more relevant and reliable measurement of the insurance liability. However under the proposed standard, and the requirements of [draft] IAS 8, an entity selecting an accounting policy for the first time would be required to look first to the main body of ED 5, which would indicate that they should apply the loss recognition test.

- We believe that this outcome was not the Board's intention. The matter can be resolved by amending Paragraph 12 to delete the word "existing" from "if an insurer's existing accounting policies do not require a loss recognition test…". In addition Paragraph 12(b) should also include a cross-reference to fair value as defined in IAS 39 (subject to our comment on Question 2 above) as an appropriate basis for measuring insurance liabilities.

Question 7 – Reinsurance purchased

We believe the proposals on the purchase of reinsurance are appropriate for Phase I, and we are supportive of the comments put forward in the Basis for Conclusions (in

Paragraphs BC 91-2). We look forward to evaluating, and to commenting on, the further proposals on reinsurance purchased that will presumably arise out of Phase II.

Question 9 – Discretionary participation features

Consistent with our response to Question 1 above, we believe that the IFRS should state more clearly the circumstances under which elements of contracts fall within IAS 39, and that where contracts do fall within IAS 39, no additional accounting guidance should then be provided within this IFRS.

Question 12 – Financial guarantees

We agree that it is appropriate that financial guarantee contracts should be considered within the scope of IAS 39.

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I hope that these comments are helpful. We would of course be very pleased to expand on any particular points if there are aspects which you find unclear, or where you would like further details of our views.

Yours sincerely

Ian Harrison

Ian Harrison
Director

LONDON INVESTMENT BANKING ASSOCIATION

LIST OF MEMBERS

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Arbuthnot Securities Limited
BNP Paribas
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