SCHEDULE 1

Form and Content of Accounts of Insurance Companies and Groups

PART I

Individual Accounts

Chapter II

Accounting Principles and Rules

Section D

Rules for Determining Provisions

Preliminary

42. Provisions which are to be shown in a company's accounts shall be determined in accordance with paragraphs 43 to 53 below.

Technical provisions

43. The amount of technical provisions must at all times be sufficient to cover any liabilities arising out of insurance contracts as far as can reasonably be foreseen.

Provision for unearned premiums

44.—(1) The provision for unearned premiums shall in principle be computed separately for each insurance contract, save that statistical methods (and in particular proportional and flat rate methods) may be used where they may be expected to give approximately the same results as individual calculations.

(2) Where the pattern of risk varies over the life of a contract, this shall be taken into account in the calculation methods.

Provision for unexpired risks

45. The provision for unexpired risks (as defined in paragraph 81 below) shall be computed on the basis of claims and administrative expenses likely to arise after the end of the financial year from contracts concluded before that date, in so far as their estimated value exceeds the provision for unearned premiums and any premiums receivable under those contracts.

Long term business provision

46.—(1) The long term business provision shall in principle be computed separately for each long term contract, save that statistical or mathematical methods may be used where they may be expected to give approximately the same results as individual calculations.

(2) A summary of the principal assumptions in making the provision under sub-paragraph (1) shall be given in the notes to the accounts.

(3) The computation shall be made annually by a Fellow of the Institute or Faculty of Actuaries on the basis of recognised actuarial methods, with due regard to the actuarial principles laid down in Council Directive 92/96/EEC.

Provisions for claims outstanding General business

47.—(1) A provision shall in principle be computed separately for each claim on the basis of the costs still expected to arise, save that statistical methods may be used if they result in an adequate provision having regard to the nature of the risks.

(2) This provision shall also allow for claims incurred but not reported by the balance sheet date, the amount of the allowance being determined having regard to past experience as to the number and magnitude of claims reported after previous balance sheet dates.

(3) All claims settlement costs (whether direct or indirect) shall be included in the calculation of the provision.

(4) Recoverable amounts arising out of subrogation or salvage shall be estimated on a prudent basis and either deducted from the provision for claims outstanding (in which case if the amounts are material they shall be shown in the notes to the accounts) or shown as assets.

(5) In sub-paragraph (4) above, "subrogation" means the acquisition of the rights of policy holders with respect to third parties, and "salvage" means the acquisition of the legal ownership of insured property.

(6) Where benefits resulting from a claim must be paid in the form of annuity, the amounts to be set aside for that purpose shall be calculated by recognised actuarial methods, and paragraph 48 below shall not apply to such calculations.

(7) Implicit discounting or deductions, whether resulting from the placing of a current value on a provision for an outstanding claim which is expected to be settled later at a higher figure or otherwise effected, is prohibited.

48.—(1) Explicit discounting or deductions to take account of investment income is permitted, subject to the following conditions:

- (a) the expected average interval between the date for the settlement of claims being discounted and the accounting date shall be at least four years;
- (b) the discounting or deductions shall be effected on a recognised prudential basis;
- (c) when calculating the total cost of settling claims, the company shall take account of all factors that could cause increases in that cost;
- (d) the company shall have adequate data at its disposal to construct a reliable model of the rate of claims settlements;
- (e) the rate of interest used for the calculation of present values shall not exceed a rate prudently estimated to be earned by assets of the company 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 shall not exceed either —
  - (i) a rate justified by the performance of such assets over the preceding five years, or
  - (ii) a rate justified by the performance of such assets during the year preceding the balance sheet date.

(2) When discounting or effecting deductions, the company shall, in the notes to the accounts, disclose —

- (a) the total amount of provisions before discounting or deductions,
- (b) the categories of claims which are discounted or from which deductions have been made,
- (c) for each category of claims, the methods used, in particular the rates used for the estimates referred to in sub-paragraph (1)(d) and (e), and the criteria adopted for estimating the period that will elapse before the claims are settled.

Long term business

49. The amount of the provision for claims shall be equal to the sums due to beneficiaries, plus the costs of settling claims.

Equalisation provision

50. Any equalisation provision established under the Insurance Companies (Credit Insurance) Regulations 1990 shall be valued in accordance with the provisions of those Regulations.

Accounting on a non-annual basis

51.—(1) Either of the methods described in paragraphs 52 and 53 below may be applied where, because of the nature of the class or type of insurance in question, information about premiums receivable or claims payable (or both) for the underwriting years is insufficient when the accounts are drawn up for reliable estimates to be made.

(2) The use of either of the methods referred to in sub-paragraph (1) shall be disclosed in the notes to the accounts together with the reasons for adopting it.

(3) Where one of the methods referred to in sub-paragraph (1) above is adopted, it shall be applied systematically in successive years unless circumstances justify a change.

(4) In the event of a change in the method applied, the effect on the assets, liabilities, financial position and profit or loss shall be stated in the notes to the accounts.

(5) For the purposes of this paragraph and paragraph 52 below, "underwriting year" means the financial year in which the insurance contracts in the class or type of insurance in question commenced.

52.—(1) The excess of the premiums written over the claims and expenses paid in respect of contracts commencing in the underwriting year shall form a technical provision included in the technical provision for claims outstanding shown in the balance sheet under Liabilities item C.3.

(2) The provision may also be computed on the basis of a given percentage of the premiums written where such a method is appropriate for the type of risk insured.

(3) If necessary, the amount of this technical provision shall be increased to make it sufficient to meet present and future obligations.

(4) The technical provision constituted under this paragraph shall be replaced by a provision for claims outstanding estimated in accordance with paragraph 47 above as soon as sufficient information has been gathered and not later than the end of the third year following the underwriting year.

(5) The length of time that elapses before a provision for claims outstanding is constituted in accordance with sub-paragraph (4) above shall be disclosed in the notes to the accounts.

53.—(1) The figures shown in the technical account or in certain items within it shall relate to a year which wholly or partly precedes the financial year (but by no more than 12 months).

(2) The amounts of the technical provisions shown in the accounts shall if necessary be increased to make them sufficient to meet present and future obligations.

(3) The length of time by which the earlier year to which the figures relate precedes the financial year and the magnitude of the transactions concerned shall be disclosed in the notes to the accounts.