Proforma-Life Limited

31 December 2008

Illustrative annual report with commentary, prepared in accordance with Schedule 9A to the Companies Act 1985 and the Association of British Insurers' Statement of Recommended Practice on Accounting for Insurance Business

Preface

PricewaterhouseCoopers' illustrative annual report for a long-term business insurance group, Proforma-Life Limited, is a practical guide to the accounting framework for UK life insurers preparing their financial statements in accordance with the requirements of Schedule 9A to the Companies Act 1985 ("CA85")[1]. The illustrative annual report considers accounting law, together with the requirements of relevant accounting standards, Urgent Issues Task Force Abstracts and other Generally Accepted Accounting Principles, current at the date of this publication[2]. Illustrative annual reports have also been prepared for a UK general insurance group under UK GAAP and for a UK composite insurance group under International Financial Reporting Standards.

Commentary boxes are provided throughout the publication, which aim to provide the reader with relevant explanations and guidance on the accounting requirements. In addition, they draw attention to the recommendations of the Association of British Insurers ("ABI") Statement of Recommended Practice on Accounting for Insurance Business ("SORP") and give an indication of our understanding of the guidance provided therein. Best-practice recommendations are provided where considered appropriate and helpful.

EU listed groups are required to prepare their consolidated financial statements using International Financial Reporting Standards ("IFRS"), rather than national GAAP. A permissive regime applies to other entities but many UK insurers are continuing to report under UK GAAP in their entity accounts, even when they are consolidated into group accounts under IFRS. Accordingly, in the shorter term, UK GAAP continues to be of relevance to many UK insurers.

These illustrative financial statements reflect all significant developments to UK GAAP for UK insurers. Proposals currently included in exposure drafts are not yet standard practice and have, therefore, not been reflected in these financial statements. In June 2008 the European Insurance CFO Forum published the Market Consistent Embedded Value (MCEV) Principles and associated Basis for Conclusions. This publication does not consider reporting of MCEV information which will usually presented as supplementary information to the financial statements.

The main changes that may impact 2008 year-ends accounts for life insurers reporting under UK GAAP are summarised below:

- **FRS 26 and FRS 29 Amendments: Financial instruments recognition, measurement and disclosures**

  In October 2008 the ASB approved an "Amendment to FRS 26 (IAS 39) and FRS 29 (IFRS 7): Reclassification of Financial Assets", that;

  - permits the reclassification of non-derivative 'held-for-trading' financial assets out of the fair value through profit or loss category in particular circumstances;
  - permits an entity to transfer loans and receivables from the AFS category to the loans and receivables category if the entity has the intention and ability to hold those loans and receivables for the foreseeable future; and
  - requires additional disclosure regarding any assets so reclassified.

  Proforma-Life has not made any such reclassifications of financial assets.

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[1] For periods beginning on or after 6 April 2008 the regulations under Companies Act 2006 apply. In particular, insurers reporting under UK GAAP will have to prepare their financial statements in accordance with the requirements of Schedule 3 to The Large and Medium sized Companies and Groups (Accounts and Reports) Regulations 2008.

[2] The accounting requirements of the UK Listing Authority's Listing Rules are not considered. Practical guidance on these Rules may be found in PricewaterhouseCoopers' Manual of Accounting.

- **Pensions accounting and disclosure**

  In December 2006 the Accounting Standards Board ('ASB') issued an amendment to FRS 17 'Retirement Benefits' to align the disclosure requirements with the equivalent international standard IAS 19. Significant additional disclosures include a reconciliation of opening and closing balances of scheme assets and of scheme liabilities and disclosure of principal actuarial assumptions. In addition, the amendment requires quoted securities to be valued at current bid-price rather than mid-market price, in line with fair value measurement of financial instruments. This amendment was effective for accounting periods beginning on or after 6 April 2007 and is reflected in these financial statements. In addition, in January 2007 the ASB published a Reporting Statement 'Retirement Benefits – Disclosures' which is designed to promote greater transparency in the reporting of pension obligations. The Statement has persuasive rather than mandatory effect. Proforma-Life has not adopted this Statement.

- **Companies Act changes**

  The Companies Act 2006 ('the Act') received Royal Assent on 8 November 2006. Implementation is being phased, with the intention of full implementation by October 2009. The changes implemented to date relate primarily to those that have immediate beneficial impact for companies' administration and do not generally impact the 2008 financial statements. The requirement to disclose in directors' reports of details of directors' interests in shares and share options was abolished in 2007. In 2008, financial statements of listed companies will have to include an enhanced business review including information on environmental, employee and social community issues. As Proforma-Life is not a quoted company it has not prepared an enhanced business review.

Future developments

2008 has primarily been a period of consolidation for UK GAAP reporting. The Accounting Standards Board ('ASB') is still considering its position in terms of how UK GAAP should progress – it has some important policy choices to make. The International Accounting Standards Board's ('IASB') convergence project with US GAAP and its implications for UK GAAP has raised a number of questions. The outcome of the IASB's IFRS for private entities project (formerly small and medium sized entities ('SME') project), is also of particular significance for UK GAAP, which now applies only to privately-owned companies. In view of these ongoing issues at the IASB, should UK GAAP continue the recent trend of harmonisation with IFRS? Alternatively should the ASB retain UK GAAP as a separate accounting framework and, if so, to what extent should this incorporate IFRS principles and standards?

During 2008 the ASB has published amendments to FRS 25, FRS 20, FRS 26 and FRS 29 in line with changes to the corresponding International Financial Reporting Standards and has also published an exposure draft of changes to certain other standards to maintain equivalence with the corresponding international standards. In addition, in February 2008 the ASB issued a discussion paper together with a brief guide that reviews the financial reporting of pensions from first principles. Among other topics, the paper considers what should be recognised in the pension liability, to whom the liability belongs, whether pension plans should be consolidated and how actuarial gains and losses should be recognised. The aim of the paper is to stimulate a debate and to influence the IASB's revision of its pensions standard.

During the year the IASB has continued to progress its project on accounting for insurance contracts. IFRS 4 currently addresses insurance accounting although this standard has not been adopted into UK GAAP, principally because it was developed very much as an interim measure and does not set out a full recognition and measurement regime. "Phase II" of the IASB insurance project on accounting for insurance contracts will address this and aims to introduce a comprehensive accounting model for insurance, tackling topics such as measurement models, up-front profit, participating contracts, credit standing, renewals and cancellation rights, asset-liability management, acquisition costs, revenue recognition and disclosure. During 2008 the IASB has commenced discussion of the responses to the 2007 discussion paper and is currently planning to issue an exposure draft in 2009 with a new standard to follow in 2011. In the meantime, until the IFRS proposals are developed, UK life insurers reporting under UK GAAP will continue to apply the guidance set out in the ABI

SORP on ‘Accounting for insurance business’ and relevant UK accounting requirements, in particular FRS 27 ‘Life insurance’.

Further guidance and information

If you require further guidance on the UK law and accounting requirements affecting insurers’ financial statements, the following PricewaterhouseCoopers publications may be of assistance:

- PricewaterhouseCoopers’ Manual of Accounting - UK GAAP 2008, published in association with Wolters Kluwer/CCH (0844 561 8166).
- The Insurance Annual Returns – A Guide through the maze. Available at a cost of £100 from Elaine Tan (020 7213 3106) or Danielle Bennett (020 7804 8129).
- Proforma-Gen Limited - Illustrative annual report under UK GAAP for a UK general insurance group. Available from Elaine Tan (020 7213 3106) or Danielle Bennett (020 7804 8129).
- Proforma Insurance (UK) plc – Illustrative annual report under International Financial Reporting Standards for a UK composite insurance group. Available from Elaine Tan (020 7213 3106) or Danielle Bennett (020 7804 8129).

If you wish to discuss any aspect of insurance financial reporting, please contact the author, Mike Vickery (0117 923 4222), or your usual PricewaterhouseCoopers contact.

PricewaterhouseCoopers LLP
London
December 2008

*It should be borne in mind that the annual report has been prepared for illustrative purposes only and shows the disclosures and formats that might be expected for an unlisted insurance group of a size similar to the Proforma-Life Group that prepares its financial statements in accordance with Schedule 9A to the Companies Act 1985, as amended by the Companies Act 1989 and subsequent statutory instruments. Accordingly, all conceivable disclosures cannot be shown and the illustrative annual report should not be used as a checklist. . The example disclosures should not be considered the only acceptable form of presentation. The form and content of each reporting entity's financial statements are the responsibility of the entity's management. Alternative presentations to those proposed in this publication may be equally acceptable if they comply with the specific disclosure requirements prescribed in UK GAAP.

These illustrative financial statements are not a substitute for reading the standards and interpretations themselves or for professional judgment as to fairness of presentation. They do not cover all possible disclosures that UK GAAP requires. The names of the undertakings and financial information, included in the annual report are used for illustration only and any resemblance to any existing undertaking is not intended. No responsibility can be accepted for loss occasioned to any person acting or refraining from action as a result of any material in this publication.

Abbreviations used

Source references used in the illustrative annual report are abbreviated as follows:

ABI, 131	Association of British Insurers' Statement of Recommended Practice ('ABI SORP') on Accounting for Insurance Business (December 2005), [paragraph number]
APB 2001/1	The Auditing Practices Board Bulletin [reference]
CA06 s234	Section number of the Companies Act 2006
FRRP PN52	Financial Reporting Review Panel Press Notice [number]
FRS 3, 14	Financial Reporting Standard [number], [paragraph number]
FSF 02/07, 11	Technical Release of ICAEW Financial Services Faculty [reference]. [paragraph number]
INSPRU 1.3.14R	Financial Services Authority's Insurance Prudential Sourcebook, [rule reference]
PwC	PricewaterhouseCoopers LLP
s234	Section number of the Companies Act 1985
ISA 700, 17	International Standard on Auditing (UK and Ireland) [number], [paragraph number]
Sch 7, 2	Schedule number to the Companies Act 1985, [paragraph number]
Sch 9A, Pt II, 2(2)	Part II of Schedule 9A to the Companies Act 1985, [paragraph number]
Sch 9A BS(4)	Note on the balance sheet format within Schedule 9A to the Companies Act 1985 [number]
Sch 9A PL(9)	Note on the profit and loss account format within Schedule 9A to the Companies Act 1985 [number]
SI1991/2128	Statutory instrument [year]/[number]
SSAP 19, 12	Statement of Standard Accounting Practice [number], [paragraph number]
Tech 1/08, 4	Technical release [number/year], [paragraph number] issued by the ICAEW and ICAS
UITF 20, 11	Urgent Issues Task Force Abstract [number], [paragraph number]

Proforma-Life Limited

s706(2)(a) (Registered Number: 187937)

Annual Report
31 December 2008

Contents

Directors and officers

Directors

W Churchill

B Disraeli

W Gladstone

D Lloyd George

H Macmillan

W Pitt (Chairman)

Reporting Actuary

H Asquith

Company Secretary

S Baldwin

Registered Office

10 Parliament Road

London

SW1 3XY

Auditors

PricewaterhouseCoopers LLP
London

s234(2)

Group directors' report for the year ended 31 December 2008

s234(1)

The directors present their report and the audited financial statements for the year ended 31 December 2008.

Principal activity

s234 ZZA (1)(b)

Sch7, 6(d)

The Company is an investment holding company and the principal activity of its subsidiary undertakings continues to be the transaction of life assurance, pensions, annuities and income protection insurance in the United Kingdom and Ireland. Complementary to these activities, the Group provides a number of other financial services, including investment and OEIC management.

Business review

The results of the Group for the year, as set out on pages 16 and 20, show a profit on ordinary activities before tax of £81.3m (2007: £78.9m). The shareholders' funds of the Group total £331.5m (2007: £296.2m).

CA06 s417

The performance of the Group during 2008 has produced encouraging results. With strong growth in the UK and Ireland, our life, pensions and retail investments have continued to exceed our expectations. Good margin and profit performance have accompanied this growth. Our focus on customer service has seen improved efficiency, allowing us to offer our customers good value products with a high quality of service. We have also seen an improvement in the amount of new business written following a review of our product offering and also as a result of the strengthening of our relationships with key independent financial advisors.

Sch7, 6(b)

On 7 July 2008 the Company acquired the whole of the issued share capital of ABC Insurance Company Limited. The Company transacts life assurance and pension business. This transaction has been accounted for as an acquisition in accordance with Financial Reporting Standard ('FRS') 6 'Acquisitions and Mergers'. Details of the fair value of the net assets acquired and the consideration paid are set out in Note 17 'Acquisition'.

Business environment

The UK life insurance industry is highly competitive. The current year has seen continuing innovation in the sector, as the industry strives to provide more flexible solutions to meet the longer term financial needs of our customers. The Group is well positioned to meet these demands and will continue to develop innovative solutions for our clients.

Strategy

The Group's success is dependent on understanding and meeting the developing needs of our customers, helping them to grow their wealth and protect their health. In the life, pensions and retail investments business, we have continued to consolidate our position. We believe it is important to retain a diversified portfolio of clients and to grow the business organically by providing a comprehensive range of long-term savings and protection products for each of our customers. We also aim to improve our new business levels through both the expansion of our distribution networks and through the continuous training and monitoring of our existing financial advisers.

The Group will continue to consolidate its position and concentrate its efforts on achieving maximum growth in its existing market segments. We aim to improve efficiency in all areas of our operations through cost reduction, motivating and retaining talented people who are committed to our goals, and by working closely with our business partners to deliver effective distribution channels. Customer service remains a top priority.

Principal risks and uncertainties

The process of risk management is addressed through a framework of policies, procedures and internal controls. All policies are subject to Board approval and ongoing review by management, risk management and internal audit. Compliance with regulation, legal and ethical standards is a high priority for the Group and the compliance team and Group finance department take on an important oversight role in this regard. The Audit Committee is responsible for satisfying itself that a proper internal control framework exists to manage financial risks and that controls operate effectively.

The Group has developed a framework for identifying the risks that each business sector, and the Group as a whole, is exposed to and their impact on economic capital. This process is risk based and uses Individual Capital Assessment principles to manage our capital requirements and to ensure we have the financial strength and capital adequacy to support the growth of the business and to meet the requirements of policyholders and regulators.

The principal risks from our life insurance business arise from being able to pay our obligations to policyholders as they fall due. Market and other risks, relating to the performance of those financial assets supporting our policyholder liabilities, are monitored by our investment board on a continuous basis.

In addition the Group is exposed to financial risks arising primarily from the investments that it holds. These risks are discussed in the section of this report dealing with financial instruments and risk management.

Future outlook

Sch7, 6(1)(b)

As the UK economy enters a period of recession there may be a change in consumer appetite for savings products given the changes in individuals' financial circumstances, uncertainty surrounding future investment returns and the impact of recent market failures on confidence in the financial sector. In such circumstances consumers will be attracted to those insurers with a demonstrably strong capital base, a portfolio of product offerings suited to changing consumer needs and an efficient cost base. We believe our strong capital base and proven track record leaves us well placed to retain our existing customers and to seek to generate new business. Notwithstanding potential difficult trading conditions we will continue to be competitive in the identification of previously uncultivated markets and offering additional products to existing customers. In addition, in the coming year we will be reviewing our cost base with a view to achieving efficiencies without reducing the levels of service provided to our policyholders.

Overall in the coming year we aim to maintain the 'annual premium equivalent' measure of new business at levels broadly consistent with the current year whilst maintaining persistency of our existing business at current levels. The level of funds under management (and consequently management charges based on the level of those funds) in the coming year will, of course, be in part dependent on investment market movements which remain a source of significant uncertainty in light of recent market conditions.

Key performance indicators ('KPIs')

We have made significant progress throughout the year in relation to key elements of our strategy. The Board monitors the progress of the Group by reference to the following KPIs:

	2008	2007 (restated)	
Annual premium equivalent	**£67.6m**	£61.1m	New regular premiums plus 1/10th of single premiums (including amounts in respect of investment contracts)
Balance on technical account	**£47.7m**	£47.1m	Balance on the long-term business technical account
Funds under management	**£3,816.9m**	£3,254.2m	Funds under management at end of year
Return on capital employed	**17.0%**	19.4%	Profit for year after tax in relation to average equity shareholders' funds
Employee retention	**98.4%**	98.9%	Number of employees at end of month (based on those in employment at the start of the month) averaged over 12 months
Customer satisfaction	The Group remains in the top quartile of the life insurers customer satisfaction survey, conducted on an annual basis by Bench & Marks, rating agency		

Business review

CA06 s417(3) The business review within the directors' report must contain:

(a) a fair review of the entity's business; and

(b) a description of the principal risks and uncertainties facing the entity.

CA06 s417(4) The business review should be a balanced and comprehensive analysis, consistent with the business' size and complexity, of:

(a) the development and performance of the entity's business during the financial year; and

(b) the position of the company at the end of the year.

The review must also include the following, to the extent necessary for an understanding of the development, performance or position of the entity's business:

(a) analysis using financial key performance indicators ('KPIs'); and

(b) where appropriate, analysis using other KPIs, including information on environmental and employee matters.

417(1), 417(8) The review must contain, where appropriate, references to and additional explanation of amounts included in the financial statements.

Best practice Where non-statutory numbers are disclosed, it should be clear that these differ from the statutory numbers, the equivalent statutory number should be disclosed and there should be a reconciliation between the statutory and non-statutory numbers.

CA06 417(1) The requirements apply to all companies, with the exception of small companies who are exempt. Insurance groups are however ineligible from the small and medium-sized companies' legislation. Small eligible subsidiaries within an ineligible insurance group may still take advantage of the exemption in their own accounts.

CA06 417(9)

Where an entity is a parent company and prepares consolidated financial statements, the business review should be a consolidated review covering the company and its subsidiary undertakings included in the consolidation. There is no requirement for the parent company to prepare a separate review for the company alone.

CA06 s417(5)

UK quoted companies are required to follow the enhanced business review reporting requirements in Companies Act 2006 for years beginning on or after 1 October 2007. The enhanced business review must include information about:

(a) the main trends and factors likely to affect the future development, performance and position of the company's business,

(b) Environmental matters

(c) The company's employees, and

(d) Social and community issues

Persons with whom the company has contractual or other arrangements which are essential to the business of the company.

Dividends

The directors have declared or proposed the following dividends:

	2008	2007
	£m	**£m**
Ordinary dividends		
- Interim paid	**8.8**	8.8
- Final proposed	**15.0**	11.4
	23.8	20.2
Preference dividends paid	**0.4**	0.4
	24.2	20.6

s234ZZA (1)(c)

Disclosure of the recommended dividend is required.

Directors

s234ZZA (1)(a)

The names of the current directors are listed on page 1. All held office throughout the year, with the exception of Mr W Churchill, who was appointed a director on 14 April 2008. Mr N Chamberlain served as a director until his retirement on 31 March 2008.

CA06 s1177

Directors' interests

Section 1177 of the Companies Act 2006 abolished the need previously present in CA85 for disclosures of directors' interests in shares and share options in directors' reports approved on or after 6 April 2007.

Qualifying third party indemnity provisions

CA06 s236(2)(3)

The directors' report should disclose whether:

(a) at the time the report is approved any qualifying third party indemnity provision (whether made by the company or otherwise) is in place for the benefit of one or more of the directors; or

(b) at any time during the year any such provision was in force for the benefit of one or more persons who were then directors.

If the company has made a qualifying third party indemnity provision and:

(a) at the time the report is approved any qualifying third party indemnity provision is in place for the benefit of one or more directors of an associated company; or

(b) at any time during the year any such provision was in force for the benefit of on or more persons who were then directors of an associated company,

(c) the report must state that such a provision is (or was) in force.

CA06 s232(2)

A qualifying third party indemnity provision is a provision by which a company directly or indirectly provides (to any extent) an indemnity for a director which meets certain conditions specified within s232(2) CA 06. For example, the definition does not include indemnity against a fine imposed by criminal proceedings pr a penalty payable to a regulatory authority in respect of non-compliance with any requirement of a regulatory nature.

Employees

Disabled persons

Sch7, 9(3)

Applications for employment by disabled persons are always fully considered, bearing in mind the respective aptitudes and abilities of the applicant concerned. In the event of members of staff becoming disabled, every effort is made to ensure that their employment with the Group continues and the appropriate training is arranged. It is the policy of the Group that the training, career development and promotion of a disabled person should, as far as possible, be identical to that of a person who does not suffer from a disability.

Employee involvement

Sch7, 11(3)

Consultation with employees or their representatives has continued at all levels, with the aim of ensuring that views are taken into account when decisions are made that are likely to affect their interests. All employees are aware of the financial and economic performance of their business units and of the Group as a whole and are rewarded according to the results of both through an annual bonus scheme. Communication with all employees continues through the in-house newspaper and newsletters, briefing groups and the distribution of the annual report.

The disclosures regarding employees are required when the average number of employees exceeds 250 each week during the financial year.

Policy and practice on payment of creditors

Sch7, 12

The Group's current policy concerning the payment of creditors, excluding amounts due in respect of the settlement of insurance and reinsurance claims, is to:

(a) agree the terms of payment with those suppliers when negotiating the terms of each transaction;

(b) ensure that those suppliers are made aware of the terms of payment by inclusion of the relevant terms in contracts; and

(c) pay in accordance with the Group's contractual and other legal obligations.

The payment policy applies to all such payments to creditors for revenue and capital supplies of goods and services without exception.

The Group's average creditor payment period at 31 December 2008 was 32 days (2007: 35 days).

Sch7, 12(1) The requirement to disclose a company's policy and practice on payment of creditors applies to UK public companies and large private subsidiaries of groups where the parent company is a UK public company. The disclosures have been given here for illustrative purposes.

PwC In the context of insurance companies, the disclosures should be made in respect of creditors for goods and services which would have been included as trade creditors had the financial statements been prepared under Schedule 4 to the Companies Act 1985 ('Schedule 4'). In particular, creditors in respect of insurance and reinsurance claims are not within the scope of the requirements.

PwC The disclosures are only required in respect of the parent company, but in view of the limited information this may convey, particularly where the parent is a non-trading holding company, we consider it best practice to include the disclosures for the group as well. Had Proforma-Life Limited been a trading parent company, it would have been appropriate to include the disclosures for both the parent company and the group.

Financial instruments and risk management

Sch7, 5A(1) Information on the use of financial instruments by the Group and its management of financial risk is disclosed in Note 1 'Management of financial risk'. In particular, the Group's exposures to price risk, credit risk and liquidity risk are separately disclosed in that note. The Group's exposure to cash flow risk is addressed under the headings of 'Interest rate risk', 'Credit risk' and 'Liquidity risk'.

Schedule 7 to the Companies Act 1985 requires disclosures in the directors' report in respect of the use of financial instruments by a company and its subsidiaries unless such information is not material for the assessment of the assets, liabilities, financial position and profit or loss. Disclosure is required of:

- financial risk management objectives and policies of the company, including the policy for hedging major forecasted transactions for which hedge accounting is used; and
- the exposure of the company and its subsidiaries to price risk, credit risk, liquidity risk and cash flow risk.

These Schedule 7 requirements overlap with the qualitative disclosure requirements of FRS 29 'Financial instruments: Disclosures' in relation to the nature and extent of risks arising from financial instruments to which the entity is exposed at the reporting date. As the disclosure requirements within FRS 29 are more extensive than the Schedule 7 requirements, all disclosures relating to the risk exposures and the management of financial risk arising from financial instruments are included within Note 1 'Management of financial risk'. It has been assumed that the requirement to disclose exposure to cash flow risk under Schedule 7 is covered by the combination of liquidity, credit and interest rate risks disclosed within Note 1, in accordance with FRS 29. The Directors' report cross-refers to these disclosures.

Charitable and political donations

Sch7, 3-5 During the year, the Group made donations to organisations engaged in cancer research of £1,500 (2006: £1,200). No donations were made for political purposes.

Donations

Sch7, 3-4 Separate disclosure is required in the directors' report of political donations within the UK/EU and in the rest of the world. If a company has made any donation to a political party in the UK or EU and/or incurred any EU political expenditure exceeding in aggregate £200 in a financial year, it will have to disclose for donations the name of each political party and the total amount given in the financial year; and for EU political expenditure, the total amount incurred in the financial year. Holding companies are also required to give the relevant disclosure for each of their subsidiaries by whom any such donation or expenditure has been made or incurred. The total amount of contributions made by a company (or group of companies) to political parties outside the EU will also require disclosure (there is no threshold for these disclosures). Wholly-owned subsidiaries of a company incorporated in Great Britain are not required to give these disclosures.

Research and development activities

Sch7, 6

An indication of the activities of the company in the field of research and development should be provided in the directors' report. A broadly-based note that considers the commercial aspects of the research and development activities and their impact on the activities of the company or group would be sufficient in most situations.

Charitable gifts

Sch7, 5

Where a company which is not a wholly-owned subsidiary of a company incorporated in Great Britain has given more than £200 for charitable purposes, the directors' report must contain, for each of the purposes for which money has been given, a statement of the amount of money given for that purpose.

Other disclosures in the directors' report

Sch 7, 1(2)

Differences between market and balance sheet value of land

If, in the opinion of the directors, the difference between the market value and the balance sheet value of land is significant, this should be disclosed. For this purpose 'land' includes buildings and other structures. The difference should be shown with such degree of precision as is practicable. There is no requirement to make a negative statement although some companies choose to do so.

Sch 7, 6(1)(a)

Post balance sheet events

Particulars should be given of any important events affecting the company or any of its subsidiary undertakings which have occurred since the balance sheet date.

FRS21, 11 and 21

FRS 21 requires disclosure of each material category of non-adjusting event after the balance sheet date. A decline in the market value of investments between the balance sheet date and the date when the financial statements are authorised for issue is given as an example of a non-adjusting event after the balance sheet date. The standard notes that abnormally large changes after the balance sheet date in asset prices would generally result in disclosure. Given the current volatility in asset prices, this disclosure requirement may be of increased relevance.

Proforma Life Limited has no disclosable post balance sheet events.

Sch 7, 7-8

Purchase of own shares and sale of treasury shares

Where the company has an interest in its own shares, the directors' report should disclose the number and nominal value of shares purchased and the percentage of the called-up share capital which those shares represent. The aggregate consideration paid and the reason for the purchase should also be given.

UITF 37

UITF Abstract 37, 'Purchases and sales of own shares' requires a company's holdings of its own shares (or in respect of group accounts holdings by subsidiaries of shares of the parent) to be accounted for as a deduction from shareholders' funds, rather than recorded as assets. Purchases and sales of own shares should be shown as changes in shareholders' funds.

CA85 4 Sch 38(1)(c)

Companies preparing accounts in accordance with Schedule 4 of Companies Act 1985 are required to disclose the number and aggregate nominal value of treasury shares held. This requirement has not been replicated in Schedule 9A for insurers. We understand this to be a drafting oversight and so believe insurers should give this disclosure as a matter of best practice.

s234ZA

Statement of disclosure of information to auditors

Each of the persons who are a director at the date of this report confirms that:

1) so far as each of them is aware, there is no information relevant to the audit of the Company's consolidated financial statements for the year ended 31 December 2008 of which the auditors are unaware; and

2) the director has taken all steps that he/she ought to have taken in his/her duty as a director in order to make him/herself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

A statement is required in the directors' report, by each of the persons who are directors at the date when the report is approved under s234A CA 85, concerning audit information given to auditors. They must state that:

(a) so far as the director is aware, there is no relevant audit information of which the company's auditors are unaware; and

(b) he has taken all the steps that he ought to have taken as a director in order to make himself aware of any relevant audit information and to establish that the company's auditors are aware of that information.

Auditors

Best practice

The auditors, PricewaterhouseCoopers LLP, have indicated their willingness to continue in office and a resolution that they be re-appointed will be proposed at the annual general meeting.

Statement of directors' responsibilities

ISA 700, 10

Company law requires the directors to prepare financial statements for each financial year that give a true and fair view of the state of affairs of the Company and the Group and of the profit or loss of the Group for that period. In preparing those financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently, with the exception of changes arising on the adoption of new accounting standards in the year;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going-concern basis, unless it is inappropriate to presume that the Group will continue in business.

The directors confirm they have complied with the above requirements in preparing the financial statements.

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the Company and the Group and enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the Company and the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

PwC

APB 2001/1

The directors' responsibilities statement is commonly included as a separate statement, within the Directors' Report (as is the case in these illustrative accounts) or at the end of any corporate governance statement. Where the financial statements are published on a website the Statement of directors' responsibilities may also include a statement that:

- the directors are responsible for the maintenance and integrity of the website; and
- legislation in the UK concerning the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

s234 A(1) By order of the Board

S Baldwin
s234 A(2) Company Secretary
3 March 2009

Company law reform

The Companies Act 2006 received Royal Assent on 8 November 2006 It represents a major overhaul of company law resulting from the Company Law Review. The Act introduces a range of measures designed to modernise and simplify company law and to make it more efficient; it also has an increased focus on corporate governance and accountability and shareholder engagement. The provisions are currently being implemented over a phased period with all provisions required to be in force by 1 October 2009.

Provisions implemented prior to April 2007

The provisions under the Companies Act 2006 which had immediate effect, or were implemented shortly thereafter, related to electronic communication, the Transparency Directive, the Takeovers Directive and those that had an immediate beneficial impact for companies' administration. These provisions included:

- Safe harbour to directors in respect of untrue or misleading statements made within the directors' reports and directors' remuneration reports provided they were not knowingly made or were reckless or, in the case of an omission, there was a dishonest concealment of facts.
- Allowing companies to use electronic communication (including e-mail and web site) to communicate with shareholders, with their consent.
- Widening the scope for electronic communication with Companies House and the Registrar of Companies and relaxing the rules for filing financial statements in a foreign language

Provisions implemented in April 2007

The Second Commencement Order related principally to the implementation of the EU Takeovers Directive. Other provisions included the removal of the disclosures in directors' reports of non-listed entities, approved on or after 6 April 2007, of directors' interests in shares and share options, following the abolition of the requirement to maintain a register of directors' interests.

Provisions implemented in October 2007

The parts of the Act implemented on 1 October 2007 included those relating to corporate governance and administration, including:

- Exercise of Members' rights
- A company's directors (other than provisions relation to directors' conflict of interest duties, directors' residential addresses and underage and natural directors)
- Derivative claims and proceedings by members
- Resolutions and meetings
- Control of political donations and expenditure
- Contents of directors' report: business review
- Fraudulent trading
- Protection of members against unfair prejudice
- Company investigations: amendments

Provisions implemented in April 2008

The provisions implemented on 6 April 2008 related to accounting and finance, as well as transactions such as reconstructions, mergers and the divisions of public companies. Other provisions implemented on this date included those relating to:

- Company secretaries
- Accounts and reports (including reduction of filing period by one month)
- Audit (most provisions including limitation of liability, personal signature of audit reports, and a statement upon appointment termination setting out the reasons).
- Right of members of quoted companies to raise audit concerns

- Debentures
- Certification and transfer of securities
- Distributions
- Arrangements and reconstructions
- Mergers and divisions of public companies
- Statutory auditors

Provisions implemented in October 2008

The provisions implemented in October 2008 relate primarily to directors' duties, appointment and share capital, as follows:

- Requirement of minimum number of natural directors, minimum age and three codified duties
- Reduction of share capital for private companies
- Acquisition of own shares – private companies

Provisions to be implemented in October 2009

The provisions to be implemented in October 2009 relate principally to the following areas:

- Re-registration of public companies as private ones procedures
- Re-denomination and reduction of share capital procedures
- Purchase of own shares
- Company's annual return – new forms required (including statement of capital)

Single regulatory regime for overseas companies with UK establishments

Independent auditors' report to the Members of Proforma-Life Limited

APB 2006/6

We have audited the Group and Parent Company financial statements (the 'financial statements') of Proforma-Life Limited for the year ended 31 December 2008 which comprise the Group Profit and Loss Account, the Group and Company Balance Sheets, the Group Cash Flow Statement, the Group Statement of Total Recognised Gains and Losses and the related notes. These financial statements have been prepared under the accounting policies set out therein.

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland). This report, including the opinion, has been prepared for and only for the Company's members as a body in accordance with Section 235 of the Companies Act 1985 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We report to you whether in our opinion the information given in the Directors' Report is consistent with the financial statements

In addition, we report to you if, in our opinion, the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Group's and Company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion:

- the financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the Group's and the Parent Company's affairs as at 31 December 2008 and of the Group's profit and cash flows for the year then ended;
- the financial statements have been properly prepared in accordance with the Companies Act 1985; and
- the information given in the Directors' Report is consistent with the financial statements.

PricewaterhouseCoopers LLP
Chartered Accountants and Registered Auditors
London, United Kingdom

3 March 2009

APB 2001/1
APB 2001/2

If the financial statements are to be posted on the company's website, further clarification of the respective responsibilities of directors and auditors is required. Unless the statement of directors' responsibilities clearly states the directors' responsibility for the maintenance and integrity of the website; and refers to the fact that uncertainty regarding legal requirements is compounded as information published on the internet is accessible in many countries with different legal requirements relating to the preparation and dissemination of financial statements, the following information should be included as notes:

- The maintenance and integrity of the entity's website is the responsibility of the directors; the work carried out by the auditors does not involve consideration of these matters and, accordingly, the auditors accept no responsibility for any changes that may have occurred to the financial statements since they were initially presented on the website.
- Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

These should appear under a heading 'Notes' at the end of the audit opinion, i.e. after the name of the auditor, place and date.

APB 2006/6

The audit report above is based on the following circumstances. In other circumstances, a different form of report would be needed.

1. Group and parent company financial statements not presented separately.
2. Company prepares group financial statements.
3. Company does not meet the Companies Act definition of a quoted company.
4. UK GAAP used for group and parent company financial statements.
5. s230 exemption taken for parent company's own profit and loss account.
6. Financial statements contain no surround information other than the directors' report.
7. Company does not voluntarily make corporate governance disclosures

Consolidated profit and loss account for the year ended 31 December 2008

Technical account – Long-term business

		Notes	2008	2007 (restated)
Sch9A, 1(1)(b)	**Earned premiums, net of reinsurance**	E	**£m**	**£m**
	Gross premiums written			
FRS 3, 14	– acquisitions	2(c)	**48.1**	–
FRS 3, 14	– other continuing operations		**353.9**	376.0
		2(a), (c)	**402.0**	376.0
	Outward reinsurance premiums		**(16.1)**	(12.2)
Sch9A, 7(3)			**385.9**	363.8
Sch9A, 2(3)	**Investment income**	G, 3	**316.4**	254.8
	Unrealised gains on investments	G, 3	**173.5**	166.5
	Other technical income, net of reinsurance	11	**27.5**	25.3
			903.3	810.4
	Claims incurred, net of reinsurance	E		
	Claims paid			
	– gross amount		**(457.3)**	(358.6)
	– reinsurers' share		**17.1**	13.1
Sch9A, 7(3)			**(440.2)**	(345.5)
	Change in the provision for claims			
	– gross amount		**(2.0)**	(1.1)
Sch9A, 7(4)			**(442.2)**	(346.6)
	Change in other technical provisions, net of reinsurance			
	Long-term business provision, net of reinsurance			
	– gross amount		**(149.6)**	(212.1)
	– reinsurers' share		**6.4**	8.9
Sch9A, 7(3)			**(143.2)**	(203.2)
	Other technical provisions, net of reinsurance			
	Technical provisions for linked liabilities	30	**(130.9)**	(101.3)
Sch9A, 7(4)			**(274.1)**	(304.5)
Sch9A, 2(3)	**Net operating expenses**	6	**(75.2)**	(65.2)
	Investment expenses and charges			
	- investment management expenses, including interest	G, 3	**(8.2)**	(6.4)
	Other technical charges, net of reinsurance		**(2.1)**	(1.1)
	Tax attributable to the long-term business	14	**(38.3)**	(26.3)
	Allocated investment return transferred to the non-technical account	G	**(10.0)**	(8.1)
	Change in present value of future profits on non-profit business written out of the with-profits fund		**4.5**	–
ABI 232	**Actuarial loss on pension scheme**	T	**(0.2)**	(0.4)
	Transfers to the fund for future appropriations	O	**(9.8)**	(4.7)
	Balance on the long-term business technical account		**47.7**	47.1

Sch9A, 1

Format of financial statements

The profit and loss account and balance sheet of insurance companies and groups preparing financial statements under UK GAAP are required to follow the formats prescribed by Schedule 9A to the Companies Act 1985 ('Schedule 9A'). For this purpose an insurance group is defined as a group where the parent company is an insurance company or where:

(a) the parent company's principal subsidiary undertakings are wholly or mainly insurance companies; and

(b) the parent company does not itself carry on any material business apart from the acquisition, management and disposal of interests in subsidiary undertakings.

Sch9A, 1, 2

Whilst Schedule 9A prescribes that items should be set out in the order and under the headings and sub-headings given in the formats, it does permit items to be disclosed in greater detail than so required. In addition, the profit and loss account and balance sheet may include items not specifically covered by the headings listed in the prescribed formats.

PwC

In these illustrative financial statements, the amounts in respect of the amortisation of goodwill and the amortisation of the present value of acquired in-force business are not material. Where such amounts are more significant, however, companies may wish to show separately on the face of the profit and loss account that element of 'other technical charges' or 'other charges', as appropriate, attributable to such amortisation. This is acceptable provided that totals for 'other technical charges' and 'other charges' are also given.

Where the format requires both gross and reinsurers' share of an amount to be given, a sub-total must also be given.

Format of profit and loss account

ABI, 225

The Proforma-Life Group does not conduct any general insurance business and as such the technical account for general business is not produced. In circumstances where the amount of general business written by a life company is not material, the ABI SORP recommends that the results should be disclosed as 'other technical income, net of reinsurance' or 'other technical charges, net of reinsurance' in the technical account for long-term business. Appropriate additional disclosure in respect of the general business is then required in the notes.

ABI, 226

It is unlikely that life mutuals will require a non-technical account, except in their group accounts where they own a material general insurance subsidiary. In such circumstances, the ABI SORP envisages the balance on the non-technical account (which will include the balance on the technical account for general business) being transferred to the technical account for long-term business, using new lines for this purpose. Where a non-insurance entity is owned by the long-term fund, the results of that entity should be included directly in the technical account for long-term business under 'other technical income' or 'other technical charges' as appropriate. Where such amounts are material, additional disclosure should be provided in the notes.

Sch9A, 2(3)

In producing the profit and loss account, the Proforma-Life Group has taken advantage of the option to combine certain items to which lower case letters in parentheses have been assigned in the profit and loss account format prescribed by Schedule 9A. Such combination is permissible if either:

(a) the individual amounts are not material for the purpose of giving a true and fair view; or

(b) the combination facilitates the assessment of the profit or loss of the company;

but is not permitted within the headings showing the derivation of net earned premiums, net claims incurred or changes in other technical provisions.

Where items are so combined as a result of (b) above, the individual amounts are required to be disclosed in the notes to the financial statements.

Sch9A, 9

Technical account – Long-term business

All contracts that are long-term business for regulatory purposes should be included in the Technical account – Long-term business. As this requirement is based on the regulatory definition it applies to all contracts regulated as insurance, including those that are accounted for as investment contracts under FRS 26. Deposits and withdrawals in relation to such contracts are accounted for on a deposit basis and are taken directly to the balance sheet. Other income and expense movements in relation to non-profit investment contracts are reflected through the Technical account – Long-term business as described below.

Aggregation of investment gains and losses

ABI, 309

The ABI SORP recommends that the headings for realised and unrealised investment gains/losses in the profit and loss account include the overall gains net of losses or losses net of gains as a single figure. In the technical account the Proforma-Life Group has made net realised gains and unrealised investment gains in both years and accordingly only the headings in respect of realised and unrealised gains are disclosed in its profit and loss account and supporting notes. Separate lines are required where losses are made in one period and gains in the other as illustrated in the non-technical account.

Other technical income, net of reinsurance

PwC

Fee income relating to non-profit investment contracts accounted for on a deposit basis under FRS 26, could appropriately be included under the technical heading "Other technical income, net of reinsurance".

Change in other technical provisions, net of reinsurance

PwC

This may include other movements in the carrying amount of financial liabilities in relation to non-profit investment contracts (other than movements relating to premiums and claims) where such amounts are classified in the balance sheet as either 'Technical provisions for linked liabilities' or 'Other technical provisions'.

Allocation of expenses

Direct and indirect expenses need to be allocated according to their source between the following four categories:

Sch9A PL(4)

(a) Claims handling expenses

ABI, 28

These will constitute part of incurred claims and will include all external and internal costs incurred in the handling of claims on insurance contracts and investment contracts with discretionary participation features.

Sch9A PL(8)

(b) Investment expenses and charges

These should be included in 'investment expenses and charges' in the technical account for long-term business or the non-technical account as appropriate and will include external and internal investment costs.

(c) Acquisition costs

Sch9A PL(6)
ABI, 20

These are reflected within net operating expenses in the technical account for long-term business and include direct costs such as acquisition commissions, and indirect costs such as advertising and the administrative expenses connected with the processing of proposals and the issuing of policies.

(d) Administrative expenses

Sch9A PL(7)
ABI, 21

These costs are reflected within net operating expenses in the technical account for long-term business and will include costs arising from premium collection, portfolio administration and inwards and outwards reinsurance, together with policy renewal commissions. They shall, in particular, include staff costs and depreciation provisions in respect of office furniture and equipment insofar as these do not need to be shown under acquisition costs, claims expenses or investment charges. Companies will need to allocate indirect costs such as staff costs, including directors' emoluments, audit fees and depreciation, between the four headings above in a logical and consistent manner that fairly reflects the running of the business.

Present value of future profits in non-profit business

PwC

In the absence of further guidance, we have included the change in present value of future profits on non-profit business written out of the with-profits fund immediately before actuarial loss on pension fund and transfer to the FFA

FRS 3, 4
ABI, 136

Analysis between continuing and discontinued operations

Discontinued operations comprise operations either sold or terminated and ceased within three months of the balance sheet date (or the date of approval of the financial statements if earlier). The operations must be material and discrete to qualify as discontinued. The ABI SORP clarifies that the cessation of writing a material category of a company's insurance business will constitute a discontinuance, provided the category comprises a discrete segment.

FRS 3, 14
ABI, 228

FRS 3 requires as the minimum disclosure on the face of the profit and loss account, an analysis of 'turnover' and 'operating profit' between continuing operations, acquisitions (as a component of continuing operations) and discontinued operations. Such analysis for each of the other statutory profit and loss account items between turnover and operating profit should be given by way of a note to the financial statements, where not disclosed on the face of the profit and loss account. For insurance undertakings the ABI SORP recommends the analysis to be restricted to those income and expenditure headings assigned with Arabic numerals in the profit and loss account format prescribed by Schedule 9A, where the amounts concerned are material.

Proforma-Life Group has not discontinued any operations in the last two years and accordingly only reference to continuing operations and acquisitions (as a component of continuing operations) is required on the face of its profit and loss account. For guidance on disclosures in respect of discontinued operations, readers should refer to the sister publication to these illustrative financial statements, Proforma-Gen Limited, dealing with the results of a general insurance group.

ABI, 306
PwC
ABI, 308

In the context of a life insurance group, the definition of operating profit is not wholly clear. In these illustrative financial statements and for the purposes of the FRS 3 analysis it has been taken to equate to profit on ordinary activities before tax and before 'super-exceptional' items (defined later), though in practice a number of companies perform the FRS 3 analysis on the balance on the long-term business technical account. Where technical results are reported based on the longer-term rate of return, the ABI SORP provides the option of disclosing operating profits based on the longer-term level of investment return. Companies may wish to analyse this measure of operating profit between continuing and discontinued activities. Analysis would be consistent with the ABI SORP requirement that where companies make an allocation of investment return, the segmental analysis should be performed on profit based on longer term investment returns.

Refer also to our commentary on supplementary disclosure of operating profit following the non-technical account.

Consolidated profit and loss account for the year ended 31 December 2008

Sch9A, 1(1)(b)

Non-Technical account

Ref		Notes	2008 £m	2007 (restated) £m
	Balance on the long-term business technical account		**47.7**	47.1
ABI, 210, 212	Tax credit attributable to balance on long-term business technical account	S, 14	**19.9**	17.3
	Shareholders' pre-tax profit from long-term business		**67.6**	64.4
	Investment income	G, 3	**8.2**	1.2
	Unrealised gains on investments	G, 3	**-**	5.8
	Allocated investment return transferred from the long-term business technical account	G, 3	**10.0**	8.1
	Investment expenses and charges			
	- investment management expenses, including interest	G, 3	**(5.5)**	(4.8)
	Unrealised losses on investments	G, 3	**(1.9)**	-
	Other income	12	**13.3**	12.7
	Other charges, including value adjustments	12	**(10.4)**	(8.5)
FRS 3, 14	Acquisitions		**3.5**	–
	Other continuing operations			
	- group		**73.6**	75.6
ABI, 276	- share of operating profit of associated undertaking		**4.2**	3.3
	Profit on ordinary activities before tax	2(c),13	**81.3**	78.9
	Tax on profit on ordinary activities	14	**(25.9)**	(22.3)
	Profit on ordinary activities after tax		**55.4**	56.6
Sch4A, 17(3) FRS 2, 35	Minority interests		**(1.9)**	(2.0)
	Profit for the financial year		**53.5**	54.6

ABI, 306

Reconciliation of operating profit based on longer term investment return to profit on ordinary activities before tax

	2008 £m	2007 (restated) £m
Operating profit based on longer-term investment return	**71.3**	70.8
Short-term fluctuations in investment return	**10.0**	8.1
Profit on ordinary activities before tax	**81.3**	78.9

Non-technical account

Tax grossing up

ABI, 210

Where the balance on the technical account is computed on an after-tax basis, the ABI SORP requires the balance to be grossed up to the pre-tax level for presentation in the non-technical account. This grossing up should be at the effective rate of tax applicable for the period as required by FRS 16. As referred to in the ABI SORP, life assurance companies are taxed on the basis of the company's overall results, such that shareholder and policyholder returns are considered together and a composite tax rate emerges. Determining the effective rate at which to gross up the transfer to shareholders from the long-term business technical account to the non-technical account is therefore difficult and the rate of grossing up might be viewed as being 'notional'. Accordingly, the ABI SORP considers that it will usually be appropriate to use the full (that is standard) rate of tax for the purposes of grossing up provided this does not result in material mis-statement of the profit before tax for the year. It is therefore necessary for directors, in preparing the financial statements, to consider whether the use of the standard as opposed to the effective rate of tax for grossing-up materially misstates the profit before tax for the year. Factors which may need to be taken into account in this consideration include:

- the availability of tax losses;
- the effect of tax planning;
- the availability of group relief; and
- the components of the aggregate tax result.

Supplementary disclosure of operating profit based on the longer-term rate of return

ABI, 360

Where technical results are reported based on the longer-term rate of return, the ABI SORP provides that supplementary disclosure may be made in the non-technical account, by way of memorandum, of the operating profit based on the longer-term level of investment return and the difference between the actual and longer-term levels of return as a result of short term fluctuations.

In these illustrative financial statements we have chosen to disclose this supplementary information by way of a footnote to the non-technical account. In circumstances where the FRS 3 analysis of operating profit is less complicated, however, because all the operations are continuing, with no acquisitions, it may be preferable to incorporate the split of operating profit in terms of the longer-term level of return and short-term fluctuations as a memorandum item within the main body of the non-technical account.

ABI, 307

Companies may also give an alternative earnings per share figure reflecting the result based on the longer-term rate of investment return.

Reporting of income from investments in participating interests

FRS 9, 27

For companies producing accounts in accordance with Schedule 4, FRS 9 'Associates and Joint Ventures' requires the investor's share of its associates' and joint ventures' operating results to be included immediately after the group operating result. This requirement conflicts with the prescribed profit and loss account format for insurance companies under Schedule 9A which requires such amounts to be included in 'income from participating interests' within investment income.

ABI, 276

The ABI SORP resolves the conflict by requiring insurance companies to follow the Schedule 9A format, but with disclosure of the aggregate share of profits/losses in relation to interests in associates and joint ventures as memorandum information on the face of the profit and loss account.

PwC

Where the associate or joint venture is owned by the long-term business fund or is a shareholder-owned associate conducting long-term business, the investor's share of its results should be included within investment income of the long-term business technical account.

The results of non-insurance, shareholder-owned associates should be included in the non-technical account.

Exceptional and extraordinary items

FRS 3, 19 FRS 3 requires all exceptional items, other than those identified as "super-exceptional" items (see below), to be included under the statutory headings to which they relate within the profit and loss account and to be disclosed separately by way of note or on the face of the profit and loss account.

FRS 3, 22 Any extraordinary profit or loss (net of tax) should be shown separately on the face of the profit or loss account, after the profit or loss on ordinary activities after taxation and minority interests but before any appropriations of

PwC profit. In practice it is not expected there will be any extraordinary item reported under FRS3, however unusual a transaction or event may be.

Proforma-Life Limited has no exceptional or extraordinary items.

Treatment of 'super-exceptional' items

FRS 3, 20 Under FRS 3 there is a requirement for so-called 'super-exceptional items', namely:

- profits or losses on the sale or termination of an operation;
- costs of a fundamental reorganisation or restructuring; and
- profits or losses on the disposal of fixed assets;

to be disclosed separately on the face of the profit and loss account. For companies preparing accounts in accordance with Schedule 4, such amounts are required to be shown after operating profit and before interest.

FRS 9, 27 There is no equivalent position in the profit and loss account format applicable to insurance companies or groups but it is industry practice to include super-exceptional items in the non-technical account immediately prior to 'profit on ordinary activities before tax'. In the case of with-profits life insurers, however, it may be necessary to include such super-exceptional items in the technical account where these items are earned or borne by the with-profits policyholders.

The investor's share of any super-exceptional items of associated undertakings should be shown separately from the amounts for the group. The results of Proforma-Life Limited, including that of its associated undertaking, do not include any super-exceptional items.

Statement of group total recognised gains and losses for the year ended 31 December 2008

FRS 3, 27

		Notes	2008	2007 (restated)
			£m	£m
	Profit for the financial year		**53.5**	54.6
	Other recognised gains and losses relating to the year			
	Exchange movements	U	**2.1**	(3.5)
FRS 17, 57	Actuarial loss on pension scheme	36	**(0.1)**	(0.4)
	Total recognised gains and losses relating to the year		**55.5**	50.7
FRS 3, 29	Prior year adjustment on adoption of amendment to FRS 17	B, 28	**(0.6)**	
	Total gains and losses recognised since last annual report		**54.9**	

FRS 3, 57

A statement of total recognised gains and losses ('STRGL') is required by FRS 3 in circumstances where any gains or losses are not reflected through the profit and loss account, i.e. are taken directly to reserves. If the company or group has no recognised gains or losses other than its profit or loss for the period, a statement to this effect should be given immediately below the non-technical account.

FRS 3, 29

In circumstances where a company or group has prior-year adjustments which impact reserves, the cumulative effect of the adjustments are required to be noted at the foot of the STRGL of the current period.

FRS 9, 28

Where an associated undertaking has gains and losses reported in its STRGL, or has such gains and losses when its accounts are restated on the investor's GAAP, the investor's share of such gains and losses should be included in the investor's consolidated STRGL. The amounts should be shown separately under each heading, if material, either in the statement or in a note referred to in the statement. The Proforma-Life Group's associated undertaking has no reported gains or losses other than those reported in its profit and loss account.

Note of historical profits and losses

FRS3, 26
FRS 3, 31a
FRS 3, 55

Neither gains and losses of an insurance group arising on the holding or disposal of investments; nor the effect of fair value accounting for financial instruments are required to be included in a note of historical profits and losses. There are no other differences between the profit on ordinary activities before tax or the profit for the financial year stated above and their historical cost equivalents.

Note of historical cost profits and losses

FRS 3, 31A

Insurance companies and groups are not required to include gains and losses arising on the holding or disposal of investments in a note of historical cost profits and losses. As a result, there will usually be no items to include in such a note.

FRS 3, 55

In addition, for the purpose of the note of historical cost profits or losses, the fair value accounting adjustments necessary under FRS 26 and hyperinflation adjustments under FRS 24 and UITF Abstract 9 are not required to be included, but this omission should be noted.

FRS 3, 28

Reconciliation of movements in group shareholders' funds for the year ended 31 December 2008

	Notes	2008	2007 (restated)
		£m	£m
Opening shareholders' funds		**296.2**	265.7
Profit for the financial year		**53.5**	54.6
Dividends on equity shares	28	**(20.2)**	(20.2)
Other recognised gains and losses relating to the year:			
- net foreign exchange differences		**2.1**	(3.5)
- actuarial (loss) recognised in the pension scheme	36	**(0.1)**	(0.4)
Net additions to shareholders' funds		**35.3**	30.5
Closing shareholders' funds		**331.5**	296.2
Included in Group shareholders' funds are aggregate net foreign exchange differences as follows:			
Aggregate net foreign exchange differences included in opening shareholders' funds		**5.7**	9.2
Net foreign exchange differences for year		**2.1**	(3.5)
Aggregate net foreign exchange differences included in closing shareholders' funds		**7.8**	5.7

Opening shareholders' funds at 1 January 2007 were originally £266.1m before deducting prior year adjustments of £0.4m in respect of the revaluation of listed investments included in pension scheme assets at bid price. This adjustment arose from the adoption of the amendment to FRS 17 'Retirement benefits'.

FRS 23, 52(b)

FRS 23 requires separate disclosure of the aggregate net exchange differences recognised through the statement of total recognised gains and losses and a reconciliation of the amount of such exchange differences at the beginning and end of the period.

FRS 3, 59

The reconciliation of movements in shareholders' funds may alternatively be disclosed in the notes to the financial statements.

Distributable profits – Tech 01/08 – Consolidated guidance on realised and distributable profits under the Companies Act 1985[3]

ICAEW and ICAS published a consolidation of their guidance on realised and distributable profits, Tech 01/08, on 25 February 2008. This superseded Techs 07/03 (Base guidance), 50/04 (Pensions), 64/04 (ESOPs and Share-based payments) and 02/07 (Recent accounting changes). The new Tech makes no changes to the previous guidance but it incorporates the updated text of Tech 07/03 made last year by Tech 02/07.

[3] Draft guidance on the determination of realised profits under the Companies Act 2006 has been issued for comment as Tech 07/08.

Tech 01/08, 3,3

Profits should be treated as realised only when realised in the form of cash or other assets the ultimate cash realisation of which can be assessed with reasonable certainty. This definition embraces profits and losses resulting from the recognition of changes in fair values, in accordance with relevant accounting standards, to the extent that they are readily convertible to cash.

Tech 01/08, 3.4

The principles of realisation set out in Tech 01/08 are relevant irrespective of whether the relevant accounts are prepared under UK GAAP or under IFRS

Tech 01/08, 3.4

In assessing whether a company has a realised profit, transactions and arrangements should not be looked at in isolation. A realised profit will arise only where the overall commercial effect on the company satisfies the definition of realised profit set out in Tech 01/08. Thus a group or series of transactions or arrangements should be viewed as a whole, particularly if they are artificial, linked (whether legally or otherwise) or circular. This principle is likely to be of particular relevance for intra-group transactions.

Tech 01/08

The guidance does not deal with the provisions in s268[4] CA 85 relating to long-term business. In some circumstances, it will be necessary to consider the interaction of s268 and Tech 01/08. For example:

PwC

- profits (included in the profit and loss account reserve in the balance sheet) arising in the long-term fund of life companies which represent amounts that have been declared as surplus in an actuarial valuation are distributable under s268 in the books of the life insurance entity. This is the case even if the profits arise from transactions of a type that Tech 01/08 would generally deem as not giving rise to distributable profits;
- where a non-insurance holding company of a life insurer receives a dividend from the life company, the holding company must consider the requirements of Tech 01/08 in determining whether the dividend represents a realised profit. In particular, where the dividend is funded, or the funding for the dividend guaranteed by, the holding company, the dividend may not give rise to distributable profits in the books of the parent company because of the circular nature of the transaction. This also applies where the parent company is a life company and the subsidiary is owned by the shareholders' fund;
- where a life company is a parent company and the long-term fund owns a subsidiary, then in assessing whether any dividends payable by the subsidiary give rise to distributable profits in the books of the parent the requirements of s268 should be applied. Thus the receipt of dividends by a long-term fund may give rise to distributable profits even if dividends of that nature would not normally be distributable under Tech 01/08; and
- profits arising in the shareholders' fund of life companies are subject to the same rules on distribution (including the requirements of Tech 1/08) as the generality of companies.

[4] Distributions made on or after 6 April 2008 are subject to the equivalent Section 843 of CA 06.

Consolidated balance sheet
at 31 December 2008

Sch9A, 1(1)(a)

	Notes	2008 £m	2007 (restated) £m
Assets			
Intangible assets			
Goodwill	H, 16	**29.1**	–
Investments			
Land and buildings	18	**180.3**	172.1
Investments in participating interests	19	**40.1**	38.2
Other financial investments	20	**1,670.0**	1,398.9
Deposits with ceding undertakings		**4.3**	2.9
	I	**1,894.7**	1,612.1
Present value of acquired in-force business	L, 21	**39.0**	–
Present value of future profits on non-profit business written out of the with-profits fund	M	**55.9**	51.4
Assets held to cover linked liabilities	22	**1,662.9**	1,415.9
Reinsurers' share of technical provisions			
Long-term business provision		**97.8**	88.1
Technical provisions for linked liabilities		**6.0**	5.9
		103.8	94.0
Debtors			
Debtors arising out of direct insurance operations	23	**45.5**	17.3
Debtors arising out of reinsurance operations		**3.1**	2.2
Other debtors		**32.1**	22.2
		80.7	41.7
Other assets			
Tangible assets	N, 24	**10.3**	10.1
Cash at bank and in hand		**62.1**	92.3
		72.4	102.4
Prepayments and accrued income			
Accrued interest and rent		**4.1**	3.9
Deferred acquisition costs	E, 25	**77.6**	59.8
Other prepayments and accrued income		**8.3**	4.1
		90.0	67.8
Total assets excluding pension asset		**4,028.5**	3,385.3
Pension asset	T	**2.2**	2.1
Total assets including pension asset		**4,030.7**	3,387.4

Sch9A, 1(1)(a)

	Notes	2008	2007 (restated)
		£m	£m
Liabilities			
Capital and reserves			
Called up share capital	27	**44.0**	44.0
Share premium account	28	**55.8**	55.8
Profit and loss account	28	**231.7**	196.4
Total shareholders' funds		**331.5**	296.2
Minority interests		**6.2**	4.3
Fund for future appropriations	O	**113.9**	89.4
Technical provisions			
Long-term business provision	P, 29	**1,626.9**	1,374.7
Claims outstanding		**16.1**	10.1
		1,643.0	1,384.8
Technical provisions for linked liabilities	Q, 30	**1,653.6**	1,411.7
Provisions for other risks and charges	31	**61.9**	47.3
Deposits received from reinsurers		**15.2**	16.0
Creditors			
Creditors arising out of direct insurance operations		**31.3**	29.2
Creditors arising out of reinsurance operations		**2.2**	1.9
Debenture loans	32	**58.5**	38.5
Amounts owed to credit institutions	32	**54.1**	21.6
Other creditors including taxation and social security	33	**39.2**	28.4
		185.3	119.6
Accruals and deferred income		**20.1**	18.1
Total liabilities		**4,030.7**	3,387.4

Sch9A, 2(3)

Consolidated balance sheet

Format of balance sheet

As with the profit and loss account (refer to commentary thereon), Proforma-Life Limited has taken advantage of the option to combine certain items in the balance sheet to which Arabic numbers have been assigned in the balance sheet format. Such aggregation is not permissible in respect of items relating to technical provisions and the reinsurers' share of technical provisions.

Called up share capital not paid

Sch9A BS(1)

Proforma-Life Limited does not have any called up share capital not paid. Where applicable, however, this asset may be disclosed either as the first asset category in the balance sheet or may be included under debtors.

Other assets

Sch9A BS(15)

Significant amounts included under the heading 'Other assets' and the sub-heading 'Other' should be analysed in the notes to the financial statements.

Present value of acquired in-force business

ABI, 198

The ABI SORP requires the present value of acquired in-force business ('PVIF') to be recognised in the acquisition balance sheet as a separate identifiable asset, and not treated as part of goodwill.

The ABI SORP defines the acquired PVIF to include two elements, being the shareholders' interest in:

ABI, 58

- the surplus emerging for distribution to shareholders from the in-force contracts; and
- surplus assets which, in practice, are not expected to be distributed to shareholders over the period of the in-force contracts. (This second element is often referred to as 'the estate'.)

PwC

The ABI SORP is silent as to the balance sheet presentation of the acquired PVIF asset. Industry practice varies, with some insurers using a new line for this purpose, whereas others include the PVIF within existing balance sheet captions, particularly in 'Other financial investments – Other'. In these illustrative financial statements we have used a new line for this purpose. The ABI SORP uses the term present value of in-force business to describe the asset recognised on acquisition. The value recognised at the date of acquisition will be a true 'present' value, but at subsequent balance sheet dates the value presented will be the value at that time of the acquired in-force business based on the acquisition date assumptions and not the value based on current assumptions (unless the asset has been subject to impairment – see commentary on Accounting policy J 'Impairment of financial assets' below). We therefore consider the use of the term 'present value' to be somewhat misleading, but have adopted the wording in these illustrative accounts on the basis that it is a recognised industry term.

Present value of future profits on non-profit business written out of the with-profits fund

FRS 27, 4(d)

FRS 27 states that within the measurement of with-profits liabilities, companies are allowed to recognise an amount in respect of the present value of future profits (PVFP) on non-profit contacts written out of the with-profits fund, provided this is also done for FSA reporting purposes and the values are those used for FSA reporting (and that the value of liabilities takes account of the value of these future profits).

The adjustments necessary to recognise the PVFP will be included in the profit and loss account with an equal and opposite transfer to the FFA. FRS 27 then sets out a number of ways that the recognised VIF may be presented:

(a) where it is possible to apportion the VIF between an amount relating to liabilities to policyholders and an amount relating to the FFA, these portions shall be presented in the balance sheet as a deduction in arriving at the amount of liabilities to policyholders and the FFA respectively;

(b) where it is not possible to make a reasonably approximate apportionment of the VIF, the amount shall be presented on the balance sheet as a separate item deducted from a sub-total of liabilities to policyholders and the FFA; or

(c) where the presentation under (a) or (b) above does not comply with statutory requirements for balance sheet presentation applying to the entity, the VIF shall be recognised as an asset.

ABI, 155 The ASB envisages that for companies reporting under UK standards and Schedule 9A to the Companies Act, legal constraints to the presentation of the balance sheet might lead to option (c) being the only permissible presentation. This is the approach adopted by Proforma-Life Limited. The ABI SORP clarifies that option (a) should be adopted but if this is not feasible, then (c) should be applied.

Assets held to cover linked liabilities

ABI, 191 Where the net assets held to cover linked liabilities at the balance sheet date differ significantly from the technical provisions for linked liabilities, the ABI SORP recommends that the reasons behind the mismatching should be disclosed. Refer also to further commentary under Note 22 ‘Assets held to cover linked liabilities’.

PwC This balance sheet heading should continue to be used for all assets held to cover linked liabilities, including those contracts which are classified as investment contracts under FRS 26.

Reinsurers’ share of technical provisions

Sch9A BS(12), (17)
ABI, 135 Schedule 9A permits the reinsurers’ share of technical provisions to be disclosed either on the asset side of the balance sheet or as a deduction from the gross amounts of the relevant technical provisions. The ABI SORP, in line with the requirements of FRS 5 ‘Reporting the Substance of Transactions’ which prohibits the netting of assets and liabilities, requires that these items are shown separately as an asset.

PwC Amounts that are recoverable under contracts that, whilst legally of the form of reinsurance, are accounted for as financial assets under FRS 26 may appropriately be shown within ‘Other financial investments’ or ‘Assets held to cover linked liabilities’ as opposed to being included within the reinsurers’ share of technical provisions.

In relation to Proforma-Life Limited, all reinsurance recoveries relate to insurance contracts.

Debtors/creditors arising out of insurance/reinsurance operations

PwC The balance sheet format within Schedule 9A requires debtors and creditors to be split between direct insurance and reinsurance operations. What is meant in this context by ‘reinsurance operations’ is not clear, but for the purposes of these illustrative financial statements we have followed the treatment adopted in insurance annual returns and interpreted debtors and creditors arising out of reinsurance operations to include balances arising from both reinsurance accepted and ceded.

Bad debt provisions

Sch9A, 34(2) Schedule 9A specifies that assets included under debtors should be shown at net realisable value. Accordingly, any provisions against reinsurance recoverables should be netted off against the associated reinsurance debts.

Deferred acquisition costs

PwC Deferred origination costs, which represent the deferral of direct incremental costs in acquiring an investment contract under FRS 26, should be included under the balance sheet heading ‘Deferred acquisition costs’ together with the deferral of acquisition costs on insurance contracts. The notes to the financial statements could analyse the balance sheet total between the amount relating to insurance contracts and with-profits investment contracts, and the amount relating to non-profit investment contracts.

PwC

Financial liabilities in relation to non-profit investment contracts

For linked contracts classified as investment contracts under FRS 26, the related financial liabilities may continue to be included within the heading ‘Technical provisions for linked liabilities’.

PwC

Where the technical provision for linked liabilities include amounts in respect of both investment contracts accounted for under FRS 26 and insurance contracts accounted for under the ABI SORP, an analysis of the technical provision between investment and insurance contracts could be given either on the face of the balance sheet or in the notes to the financial statements.

PwC

For any non-linked non-profit investment contracts, the related financial liabilities could be included within ‘Other technical provisions’ or ’Other creditors, including tax and social security’. Alternatively a case could be made for creating a new line for non-linked financial liabilities in respect of such investment contracts within the balance sheet format, as permitted by Schedule 9A s.2(2), on the grounds that they are not “specifically included” in any of the existing captions.

Proforma-Life Limited has unit-linked investment contracts under FRS 26 and has included the related financial liabilities under ‘Technical provisions for linked liabilities’. The Group has no non-linked non-profit investment contracts.

Disclosure of long-term business unrealised profits within reserves

Sch9A, 10(1)

Schedule 9A requires the balance sheet of a company which carries on long-term business to show separately as an additional item the aggregate of any amounts included in capital and reserves which are not realised profits as defined by s268 CA85. We understand that this disclosure is required in order to avoid non-distributable profits being included in the profit and loss account without appropriate disclosure.

This situation is likely to arise where profits are retained in the long-term business fund for solvency purposes under the FSA Handbook, but are included in the transfer to the non-technical account in the Companies Act accounts as a result of the application of the modified statutory solvency basis of reporting.

Sch9A, PtII, 2(2)

This disclosure is not required in respect of the consolidated balance sheet.

Provision for unearned premiums

Sch9A BS(20)

In the case of long-term business, the provision for unearned premiums may either be shown as a separate technical provision or included within the calculation of the long-term business provision. For the purposes of Proforma-Life Limited financial statements, the latter option has been taken.

Deferred income

PwC

Initial fee income which is deferred and recognised in line with the performance of the related contract should be included in the balance sheet as ‘Accruals and deferred income’.

Sch4, 1(1)(a)

Balance sheet of the company at 31 December 2008

	Notes	2008	2007
Fixed assets		**£m**	**£m**
Investments			
Shares in group undertakings		**330.6**	235.1
Loans to group undertakings		**21.3**	31.3
	I, 19	**351.9**	266.4
Current assets			
Debtors			
Amounts owed by group undertakings		**37.4**	30.0
Other debtors		**4.3**	4.1
		41.7	34.1
Investments		**5.1**	2.1
Cash at bank and in hand		**–**	4.2
		46.8	40.4
Creditors: amounts falling due within one year			
Bank loans and overdrafts	32	**(39.3)**	(2.1)
Amounts owed to group undertakings		**(3.1)**	(2.3)
Other creditors including taxation and social security	33	**(4.1)**	(3.3)
		(46.5)	(7.7)
Net current assets		**0.3**	32.7
Total assets less current liabilities		**352.2**	299.1
Creditors: amounts falling due after more than one year			
Debenture loans	32	**(58.5)**	(38.5)
Amounts owed to group undertakings		**(18.6)**	(7.3)
		(77.1)	(45.8)
		275.1	253.3
Capital and reserves			
Called up share capital	27	**44.0**	44.0
Shared premium account	28	**55.8**	55.8
Profit and loss account	28	**175.3**	153.5
Total shareholders' funds		**275.1**	253.3

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The financial statements on pages 16 to 135 were approved by the Board of directors on 3 March 2009 and were signed on its behalf by:

W Pitt
Chairman

Where the holding company is not itself an insurance company, as is the case here, its balance sheet should be prepared in accordance with Schedule 4, not Schedule 9A, to the Companies Act 1985.

FRS 1

Consolidated cash flow statement
for the year ended 31 December 2008

		Notes	2008 £m	2007 (restated) £m
FRS 1, 7	**Net cash inflow from operating activities**	35 (a)	**58.6**	49.2
FRS 1, 7	**Returns on investments and servicing of finance**			
FRS 1, 15(a)	Interest paid		**(4.7)**	(2.9)
FRS 1, 15(d)	Non-equity dividends paid		**(0.4)**	(0.4)
FRS 1, 15(e)	Dividends paid to minority interests		**(0.3)**	(0.2)
			(5.4)	(3.5)
FRS 1, 7	**Taxation**			
FRS 1, 18	Corporation tax paid		**(21.5)**	(17.3)
FRS 1, 7	**Acquisitions**			
FRS 6, 33	Acquisition of subsidiary undertaking	35 (e)	**(95.5)**	–
FRS 1, 24(a)	Net cash acquired with subsidiary undertaking	35 (e)	**1.4**	–
			(94.1)	–
FRS 1, 7	**Equity dividends**			
FRS 1, 29	Equity dividends paid	28	**(20.2)**	(20.2)
FRS 1, 7	**Financing**			
FRS 1, 30(b)	Increase in borrowings	35 (d)	**47.2**	15.1
	Net cash (outflow)/inflow		**(35.4)**	23.3
FRS 1, 35	**Cash flows were (applied)/invested as follows:**			
	Net portfolio investments			
	Shares and other variable-yield securities	35 (d)	**(12.9)**	9.8
	Loans, debt securities and other fixed income securities	35 (d)	**(1.1)**	1.6
	Deposits with credit institutions	35 (d)	**(1.1)**	0.8
		35 (c)	**(15.1)**	12.2
	(Decrease)/increase in cash holdings	35 (d)	**(20.3)**	11.1
	Net (application)/investment of cash flows		**(35.4)**	23.3

Cash flow statement

FRS 1, 36

Recognising that shareholders of an insurance company generally only have restricted rights to any profits, and associated cash surpluses, made by the long-term business, FRS 1 requires the long-term business cash flows to be included in the cash flow statement only to the extent of cash transferred to, and available to meet the obligations of, the company or group as a whole.

Similar considerations apply to mutual life assurance companies that are owned by the policyholders and they are accordingly exempt from the requirements of the FRS.

FRS 1, 12

A reconciliation between operating profit and the net cash flow from operating activities should be presented either adjoining the cash flow statement or as a note. In the accounts of the Proforma-Life Limited, the reconciliation is provided in Note 35(a). Where presented immediately following the cash flow statement, it should be clearly labelled and kept separate.

FRS 1, 35

Instead of the normal requirement to include a section in the cash flow statement relating to the ‘management of liquid resources’, insurance companies or groups are required to include a section relating to ‘portfolio investments’. This format recognises the special nature of insurance business, in particular the importance of generating resources for investment to meet provision requirements for future claims and reserve requirements for solvency.

FRS 1, 35

In view of the fact that the balance sheet format in Schedule 9A does not distinguish between fixed and current assets, an analysis of the movement in portfolio investments less financing is required, instead of the normal requirement to analyse the movement in net debt. This reconciliation is not intended to form part of the cash flow statement and accordingly, where presented immediately following the cash flow statement, it should be clearly labelled and kept separate.

Sch9A, 55

Statement of accounting policies

FRS 18 'Accounting policies'

FRS 18

FRS 18 sets out the principles to be followed in selecting accounting policies and the disclosures needed to help users to understand the accounting policies adopted and how they have been applied. It distinguishes between accounting policies and estimation techniques.

FRS 18, 4

Accounting policies are:

- those principles, bases, conventions, rules and practices applied by an entity that specify how the effects of transactions and other events are to be reflected in its financial statements through:

(i) recognising;
(ii) selecting measurement bases for; and
(iii) presenting;

Assets, liabilities, gains, losses and changes to shareholders' funds. Accounting policies do not include estimation techniques.

Accounting policies define the process whereby transactions and other events are reflected in financial statements.

FRS 18, 4

Estimation techniques are:

- the methods adopted by an entity to arrive at estimated monetary amounts, corresponding to the measurement bases selected, for assets, liabilities, gains, losses and changes to shareholders' funds.

Estimation techniques implement the measurement aspects of accounting policies. An accounting policy will specify the basis on which an item is to be measured; where there is uncertainty over the monetary amount corresponding to that basis, the amount will be arrived at by using an estimation technique.

FRS 18, 14-17

Accounting policies should be consistent with accounting standards, UITF Abstracts and companies' legislation. Where this requirement allows a choice, the FRS requires an entity to select those accounting policies judged to be most appropriate to its particular circumstances for the purpose of giving a true and fair view.

FRS 18, 30-31

An entity should judge the appropriateness of accounting policies to its particular circumstances against the objectives of relevance, reliability, comparability and understandability. The constraints that an entity should take into account are the need to balance the different objectives, and the need to balance the cost of providing information with the likely benefit of such information to users of the entity's financial statements.

FRS 18, 51

Where it is necessary to choose between estimation techniques, an entity should select whichever of those estimation techniques is judged by the entity to be most appropriate to its particular circumstances for the purpose of giving a true and fair view.

FRS 18, 45

An entity's accounting policies should be reviewed regularly to ensure that they remain the most appropriate to its particular circumstances. An entity should implement a new accounting policy if it is judged more appropriate to the entity's particular circumstances than the present accounting policy.

Disclosure requirements

FRS 18, 55 The FRS requires specific disclosures about the accounting policies followed and changes to those policies. The following information should be disclosed:

(a) a description of each of the accounting policies that is material in the context of the financial statements;

(b) a description of those estimation techniques adopted that are significant;

(c) details of any changes to the accounting policies that were followed in preparing financial statements for the preceding period, including:

    (i) an explanation of why each new accounting policy is thought more appropriate;
    (ii) where practicable, the effect of a prior period adjustment on the results for the preceding period, in accordance with FRS 3; and
    (iii) where practicable, an indication of the effect of a change in accounting policy on the results for the current period.

    Where it is not practicable to make the disclosures described in (ii) or (iii), that fact, together with the reasons, should be stated;

(d) where the effect of a change to an estimation technique is material, a description of the change and, where practicable, the effect on the results for the current period.

FRS 18, 58 Where an entity's financial statements fall within the scope of a SORP, the entity should state the title of the SORP and whether its financial statements have been prepared in accordance with the provisions of the SORPs currently in effect. In the event of a departure, disclosure is required of how the financial statements depart from the recommended practice set out in the SORP. This disclosure should include:

(a) for any treatment that is not in accordance with the SORP, the reasons why the treatment adopted is judged more appropriate to the entity's particular circumstances; and

(b) details of any disclosures recommended by the SORP that have not been provided, and the reasons why they have not been provided.

FRS 18, 62 For any material departure from the requirements of an accounting standard, a UITF Abstract or companies legislation, particulars of the departure, the reasons for it and its effect should be disclosed. The disclosure should include:

(a) a clear statement that there has been a departure from the requirements of an accounting standard, a UITF Abstract or companies legislation, and that the departure is necessary to give a true and fair view;

(b) a statement of the treatment that the accounting standard, UITF Abstract or companies legislation would normally require in the circumstances and a description of the treatment actually adopted;

(c) a statement of why the treatment prescribed would not give a true and fair view; and

(d) a description of how the position shown in the financial statements is different as a result of the departure, normally with quantification. Quantification is not required where it is already evident in the financial statements themselves or where the effect cannot reasonably be quantified, in which case the circumstances should be explained.

Estimation techniques

Clearly in the case of insurance there is often uncertainty over the monetary amount corresponding to the recognition and measurement of claims. Accordingly the requirements of FRS 18 in connection with estimation techniques are of particular relevance to insurers. FRS 18 requires:

FRS 18, 50

- that where estimation techniques are required to enable the accounting policies adopted to be applied, an entity should select estimation techniques that enable its financial statements to give a true and fair view and are consistent with the requirements of accounting standards, UITF Abstracts and companies legislation;

FRS 18, 51 PwC

- where it is necessary to choose between estimation techniques that satisfy these conditions, an entity should select whichever of those estimation techniques is judged by the entity to be most appropriate to its particular circumstances for the purposes of giving a true and fair view. For long-term insurers we consider that regard should also be had to the ABI SORP in the selection of appropriate estimation techniques;

FRS 18, 55(b)

- description of those estimation techniques that are significant. This is considered further below; and

FRS 18, 57 ABI, 244

- where the effect of a change to an estimation technique is material, a description of the change and, where practicable, the effect on the results for the current period. This is considered further below.

FRS 18, 57

FRS 18, paragraph 57 explains that:

ABI, 243

- although many estimation techniques are used in preparing financial statements, most do not require disclosure because, in most instances, the monetary amounts that might reasonably be ascribed to an item will fall within a relatively narrow range. An estimation technique is significant for the purposes of paragraph 55 (b) only if the range of reasonable monetary amounts is so large that the use of a different amount from within that range could materially affect the view shown by the entity's financial statements;
- to judge whether disclosures are required in respect of a particular estimation technique, an entity will consider the impact of varying the assumptions underlying that technique; and
- the description of a significant estimation technique will include details of those underlying assumptions to which the monetary amount is particularly sensitive.

ABI, 238 PwC ABI, 184-191

In respect of long-term insurance business, the estimation techniques for determining technical provisions are likely to be significant. Accordingly, FRS 18 requires a description of the estimation techniques employed including details as to those individual underlying assumptions to which the technical provisions amounts are particularly sensitive. The ABI SORP provides guidance on the disclosure of uncertainties and estimation techniques in respect of insurance contracts. It also provides definitions of the estimation techniques commonly used. There are various disclosure requirements in the ABI SORP (particularly at paragraphs 184 to 191) in connection with the determination of technical provisions for long-term business, which assist in meeting the requirements of FRS 18.

PwC

The requirements of FRS 27 give rise to significant areas of estimation. For example, the calculation of realistic liabilities includes estimates in respect of future bonuses. The use of stochastic modelling for calculating the cost of options and guarantees includes estimates such as market consistent expected return and the volatility of those expected returns.

ABI, 239, 242

There is inherent uncertainty in estimating many of the technical provisions in respect of liabilities arising from insurance business. They can be classified as:

- general uncertainties with 'normal' ranges of outcomes. These should be described in the accounting policies and periodically reviewed;
- specific uncertainties which are material and subject to an unusually wide ranges of outcomes. When the possibility of a range of outcomes is outside the 'normal' range, separate disclosure should be made. Disclosure should include the circumstances, indication of uncertainties, amount and timing of the outflows and the possibility of any related reimbursements; and
- uncertainties in areas where FRS 12 does not require a provision to be established but where that standard may require contingent liability disclosure.

ABI, 240

FRS 18 requires the following disclosures in the financial statements:

- a broad description of the factors giving rise to the uncertainty;
- a description of those items to which significant estimation techniques have been applied;
- a description of the estimation techniques used;
- details of the significant assumptions made and information used in forming the estimates; and
- a note of those factors to which the estimation technique is particularly sensitive.

ABI, 245-247

Provisions, contingent liabilities and contingent assets arising from insurance contracts with policyholders are exempt from the requirements of FRS 12 and, in the majority of circumstances, the level of disclosure required by FRS 18 will be appropriate. However, where a specific material contingent liability exists in respect of which no provision has been made in the financial statements, and the prospect of this resulting in a transfer of economic benefits is more than remote, it will be appropriate to give the level of disclosure that would be required by paragraph 91 of FRS 12.

A. Basis of presentation

FRS 18, 58
ABI, 313

The Group financial statements have been prepared in accordance with the provisions of s255A of, and Schedule 9A to, CA 85, and with the Statement of Recommended Practice on Accounting for Insurance Business issued by the Association of British Insurers ('the ABI SORP') in December 2005 and revised in December 2006. The balance sheet of the holding company has been prepared in accordance with s226 of, and Schedule 4 to, the Companies Act 1985.

Sch9A, 56

The financial statements have been prepared in accordance with applicable accounting standards. A summary of the more important Group accounting policies is set out below, together with an explanation of where changes have been made to previous policies on the adoption of new accounting standards in the year.

Compliance with Statement of Standard Accounting Practice ('SSAP') 19 'Accounting for investment properties' requires departure from the requirements of the Companies Act 1985 relating to depreciation and an explanation of the departure is given in Accounting policy I 'Investments' below.

B. Changes in accounting policies

The Group has adopted the amendment to FRS 17 'Retirement benefits' in full in these financial statements. As well as changing certain disclosures (where comparatives have been restated accordingly), The adoption of this amendment has given rise to a change in accounting policy in respect of the valuation of listed equity investments and bonds which are held in scheme assets which are now valued at the current bid price, having previously been valued at mid-market value. The effect of this change in accounting policy was to reduce profit before tax and profit after tax by £0.1m (2007: £0.2m). Note 28 Share premium account and reserves details the effect of this change on opening reserves.

FRS 29, 43
FRS 18, 55

Following a change in accounting policy, a brief explanation is required of why each new accounting policy is thought to be more appropriate, and, where practicable, an indication of the effect of a change in accounting policy on the results for the current period. If it is not practicable to make this disclosure, that fact, together with the reasons, should be stated.

FRS 3, 29

The amounts for the corresponding period should be restated on the basis of the new policy and the effect on the results for the preceding period should be disclosed where practicable. Where it is not practicable to make this disclosure, that fact, together with the reasons, should be stated.

FRS 18, 55 Where the effect of a change to an estimation technique is material, a description of the change and, where practicable, the effect on the results for the current period should be disclosed. Proforma-Life Limited and its FSA regulated subsidiaries have chosen to adopt changes to the method of calculating liabilities to insurance contract policyholders as permitted by the FSA Instrument ‘Prudential Requirements for Insurers (Amendment) Instrument 2006’ (FSA 2006/62). This represents a change to an estimation technique and appropriate disclosure is made within Accounting policy P ‘Long-term business provision’ and Note 29 ’Long-term business provision’.

A change to an estimation technique should not be accounted for as a prior period adjustment, unless it represents the correction of a fundamental error or the change is required to be accounted for as a prior period adjustment by another accounting standard, a UITF Abstract or companies’ legislation.

C. Basis of consolidation

ABI, 270 The consolidated financial statements incorporate the assets, liabilities and results of the Company and its subsidiary undertakings drawn up to 31 December each year. The results of subsidiary undertakings acquired or sold during the period are included in the consolidated results from the date of acquisition or up to the date of disposal. On the acquisition of a subsidiary undertaking, all of its assets and liabilities at the date of acquisition are recorded at their fair values reflecting their condition at that date.

ABI, 274 Associated undertakings are companies, other than subsidiary undertakings, in which the Group holds 20% or more of the equity share capital for the long term and over which the Group exercises significant influence. Associated undertakings are accounted for using the equity methods of accounting.

ABI, 271 In circumstances where an investment in a group undertaking belongs to the long-term business, changes in the value of which affect or establish policyholders’ rights, the Companies Act 1985 prohibits adjustments being made to the related insurance liabilities in the consolidated accounts. Where the current value exceeds or is less than the net assets consolidated, the difference should be included as an additional asset or liability in the balance sheet, using a new line for this purpose.

Interests in associates and joint ventures

ABI, 272 The ABI SORP gives guidance on the accounting treatment of interests in associates and joint ventures. Such interests forming part of an investment portfolio within the meaning of paragraph 50 of FRS 9 should be included in the financial statements of both the parent undertaking and the group as investments in the same way as other investments within the portfolio.

ABI, 273 In the case of the Proforma-Life Group, the interest in its associated undertaking is an operational interest. The ABI SORP states that such interests should be accounted for in the parent undertaking’s and the group’s balance sheet using the prescribed caption ‘Investments in group undertakings and participating interests’. In the group balance sheet the valuation method which is adopted is the equity or gross equity basis as required by FRS 9.

ABI, 276 As noted in the commentary on the non-technical account, the Schedule 9A requirements in respect of the profit and loss account presentation are at odds with the FRS 9 requirements. Insurers should therefore include the amounts in the profit and loss account under ‘Investment Income: Income from participating interests’ and disclose as a memorandum item in the non-technical account the amount of the group operating result attributable to the share of operating results of associates and joint ventures.

D. Contract classification

The Group issues contracts that transfer insurance risk or financial risk or both.

Insurance contracts are those contracts that transfer significant insurance risk. Such contracts may also transfer financial risk. As a general guideline, the Group defines as significant insurance risk the possibility of having to pay benefits on the occurrence of an insured event that are at least 10% more than the benefits payable if the insured event did not occur. A contract classified as an insurance contract continues to be treated as such until all rights and obligations under the contract expire.

Investment contracts are those contracts that transfer financial risk with no significant insurance risk.

Unit-linked contracts written by the Group, where the liability under the contract is dependent on the value of the underlying financial assets, derivatives and/or investment property, are classified as investment contracts unless the contracts also contain features that transfer significant insurance risk.

All with-profits contracts contain a discretionary participation feature ('DPF') which entitles the holder to receive, as a supplement to guaranteed benefits, additional benefits or bonuses:

- that are likely to be a significant portion of the total contractual benefits;
- whose amount or timing is contractually at the discretion of the Group; and
- that are contractually based on:
  - (i) the performance of a specified pool of contracts or a specified type of contract;
  - (ii) realised and/or unrealised investment returns on a specified pool of assets held by the Group; or
  - (iii) the profit or loss of the Group, fund or other entity that issues the contract.

The terms and conditions of these contracts, together with UK regulations, set out the bases for the determination of the amounts on which the additional discretionary benefits are based and within which the Group may exercise its discretion as to the quantum and timing of their payment to contract holders.

With-profits contracts are classified as either insurance contracts or investment contracts depending on the level of insurance risk transferred.

All non unit-linked non-profit contracts issued are insurance contracts.

FRS 26, 2(e)

FRS 26 does not apply to rights and obligations under an insurance contract or under a contract containing a discretionary participation feature. The definition of an insurance contract, and of a discretionary participation feature, and the associated guidance from IFRS 4 'Insurance contracts", have been included in Appendix C to FRS 26. Under FRS 26 insurance products have to be classified between insurance contracts and investment contracts. The measurement requirements of FRS 26 apply to non-profit investment contracts whereas insurance contracts and with-profits investment contracts continue to follow the existing provisions of the ABI SORP and FRS 27 to determine accounting treatments. The disclosure requirements of FRS 29 will apply to all investment contracts (including with-profits investment contracts).

Unbundling of contracts

PwC

Where a direct contract contains both an investment element and an insurance element (for example, hybrid contracts or contract riders), there is currently no guidance under UK GAAP on whether the contract should or may be unbundled. The guidance within IFRS 4, which allows the investment contract portion of such contracts to be accounted for separately under IAS 39 using deposit accounting whilst continuing to account for the insurance element under IFRS 4, is not replicated in FRS 26 (although reference is made to unbundling in the context of significant insurance risk, in Appendix C para 34).

FRS 5 'Reporting the substance of transactions' aims to ensure that the substance of an entity's transactions is faithfully represented in the financial statements. Furthermore, the ABI SORP para 255 addresses the unbundling of reinsurance contracts in relation to FRS 5 and states that "any reinsurance contract should be accounted for in two parts where elements can be identified that do not result in the transfer of significant insurance risk". The ABI SORP remains silent on the unbundling of direct insurance contracts. In the absence of any specific guidance, the practice of unbundling direct insurance contracts does not appear to contravene UK GAAP.

Proforma-Life Limited has not chosen to unbundle direct insurance contracts.

E. Insurance contracts and with-profits investment contracts

Premiums

ABI, 163, 165 Premiums, including reinsurance premiums, and consideration for annuities are accounted for when due for payment, except for unit-linked premiums, which are accounted for when units are created.

ABI, 162 Premiums written do not include premiums in relation to investment contracts under FRS 26. Deposit accounting is used for such non-profit investment contracts which involves recognising the consideration received as a liability rather than as revenue.

ABI, 163 Where the amount due is not known, for example with certain pensions business, estimates should be used.

Claims

ABI, 166 Maturity claims and annuities are charged against revenue when due for payment.

ABI, 167 Surrenders are accounted for when paid or, if earlier, on the date when the policy ceases to be included within the calculation of the long-term business provision and/or the technical provisions for linked liabilities.

ABI, 166 Death claims and all other claims are accounted for when notified.

ABI, 168 Claims payable include related internal and external claims handling costs.

Acquisition costs

FRS 27, 4(b) The costs of acquiring new business that is not written out of the with-profits fund, and which are incurred during a financial year but expected to be recoverable out of future revenue margins, are deferred. Such costs are disclosed as an asset in the balance sheet, gross of tax, and are determined explicitly. For business written within the with-profits fund, acquisition costs are not deferred.

ABI, 177 The deferred acquisition cost asset is amortised over the period in which the costs, net of the related deferred tax provision, are expected to be recoverable out of margins in matching revenues from the related policies. The rate of amortisation is consistent with the pattern of emergence of such margins.

In respect of linked business, amortisation of the deferred acquisition cost asset commences on the recognition of premiums available to meet costs as provided in the contractual terms of the policy.

Sch9A BS(17) Schedule 9A requires the cost of acquiring insurance policies which are incurred during a financial year, but which relate to a subsequent financial year, to be deferred as an explicit asset in the balance sheet, except to the extent that such costs are explicitly or implicitly recognised in the computation of the long-term business provision.

FRS 27, 4(c) FRS 27 states that 'For with-profits funds falling within the scope of the FSA realistic capital regime… acquisition costs shall not be deferred'.

ABI, 170 The ABI SORP states that acquisition costs should be deferred explicitly. Such a deferred acquisition cost asset may be calculated in whole or in part by means of an actuarial method (e.g. zillmerisation) which, in making allowance in the computation of the long-term business provision or the technical provisions for linked liabilities

ABI, 171 for such deferred costs, enables the costs so deferred to be separately identified and disclosed. Advertising costs should not be deferred unless they relate directly to the acquisition of new business.

ABI, 172 The full amount of the deferred acquisition costs should be included as an asset in the balance sheet after adjusting, where appropriate, for any deferred tax liability recognised automatically in the actuarial valuation. A deferred tax provision should then be established where appropriate in accordance with the requirements of FRS 19 'Deferred Tax' and the long-term business provision grossed up by the amount of any zillmerisation deduction allowed for in the actuarial valuation.

Policyholder liabilities under insurance contracts and with-profits investment contracts

See Accounting policies P 'Long-term business provision' and Q 'Technical provisions for linked liabilities'.

Reinsurance

ABI, 250-251 Long-term business is ceded to reinsurers under contracts to transfer part or all of one or more of the following risks: mortality, morbidity, investment, persistency and expenses. Such contracts are accounted for as insurance contracts provided the risk transfer is significant. Some contracts which provide for the transfer of significant risk are also structured to provide financing. When, under such contracts, financing components are to be repaid in future accounting periods, the amount outstanding under the contract at the balance sheet date is classified as a liability to the reassurer and included in 'deposits received from reinsurers'. Contracts with the legal structure of reinsurance contracts which do not transfer significant insurance risk are classified as financial assets.

The amounts that will be recoverable from reinsurers are estimated based upon the gross provisions, having due regard to collectability. The recoverability of reinsurance recoveries is assessed having regard to market data on the financial strength of each of the reinsurance companies. The reinsurers' share of claims incurred, in the profit and loss account, reflects the amounts received or receivable from reinsurers in respect of those claims incurred during the period. Reinsurance liabilities are primarily premiums payable for reinsurance contracts and are recognised in the profit and loss account as 'Outwards reinsurance premiums' when due.

ABI, 249-250 In accordance with FRS 5, the economic substance of all reinsurance contracts must be reflected in the result for the year and the balance sheet. A key characteristic of reinsurance is the transfer and assumption of reinsurance risk and so reinsurance contracts that do not transfer significant risk should not be accounted for as contracts of reinsurance, but should be treated as financial instruments under FRS 26.

PwC When considering the accounting treatment of reinsurance contracts ceded that transfer all the risks of the underlying contracts, it is appropriate to have regard to the FRS 26 classification of the underlying contracts accepted in order to achieve accounting symmetry.

ABI, 255 Where a reinsurance contract contains identifiable elements that do not result in the transfer of insurance risk, these should be separately accounted for.

ABI, 257 In determining whether assets and liabilities should be recognised, the following three stage process is to be followed:

- consideration of the transaction in conjunction with any other where this is necessary to obtain an understanding of the overall commercial effect;
- determination of the reasonably possible outcomes of the transaction having regard to its commercial effect, uncertainty, and the intentions of the parties to the transaction insofar as these assist in determining its substance; and
- assessment of whether assets and/or liabilities have been created based on the above stages.

ABI, 260 Assets created by reinsurance contracts should normally be valued on the same basis as the related reinsured liabilities, subject to any allowance for bad debt.

ABI, 39 Where a reinsurance contract is intended, in whole or in part, to mitigate the requirement to establish prudent provisions, and/or to provide an element of financing, the identifiable elements of the contract which do not transfer significant insurance risk are considered to be financial reinsurance.

ABI, 261 Where material, any financial reinsurance element should not result in a net credit to the profit and loss account on inception of the contract, even where the main purpose of a reinsurance contract is the transfer of insurance risk.

ABI, 262 Disclosure of reinsurance contracts should enable a full understanding of their effect on the results in the financial statements.

F. Unit-linked investment contracts

Amounts received in respect of unit-linked investment contracts, which principally involve the transfer of financial risk, are accounted for using deposit accounting, under which amounts collected are credited directly to the balance sheet, as an adjustment to the liability to the policyholder. Financial liabilities in respect of unit-linked investment contracts are carried in the balance sheet as 'Technical provisions for linked liabilities' (see Accounting policy Q 'Technical provisions for linked liabilities').

Fees receivable from unit-linked investment contracts (included in 'Other technical income') and investment income and interest payable on contract balances are recognised in the profit and loss account in the year they are assessed unless they relate to services to be provided in future years, in which case they are deferred and recognised as the service is provided.

Incremental costs that are directly attributable to securing unit-linked investment contracts, and are expected to be recoverable, are deferred and recognised in the balance sheet as deferred acquisition costs. The asset is amortised as the related fees for investment management services are recognised.

Valuation of financial liabilities in respect of non-profit investment contracts

PwC Where an insurer issues investment contracts that fall within the scope of FRS 26 the financial liabilities in respect of such contracts must be measured in accordance with that standard i.e. at amortised cost or, provided certain criteria are met, at fair value through the profit and loss account under "the fair value option". However, the provisions of Schedule 9A para 29A, which allow financial instruments to be included at fair value within UK GAAP financial statements, do not apply to financial instruments which constitute liabilities unless:

(a) they are held as part of a trading portfolio; or

(b) they are derivatives.

This is interpreted as meaning that (unless the use of fair value to measure the financial liabilities in question is explicitly permitted elsewhere in Schedule 9A) the fair value measurement of financial liabilities (other than derivatives) that are not held as part of a trading portfolio is not consistent with the requirements of Schedule 9A.

Any use of the fair value option that is a departure from the requirements of Schedule 9A will require a true and fair override. FRS 18 requires disclosure of the particulars, reasons and effect where a departure from the Companies Act 1985 has been made in order to give a true and fair view.

Unit-linked investment contract liabilities

PwC

It is likely that, under FRS 26, life insurance companies will seek to measure unit-linked investment contract liabilities on a basis consistent with the related unit-linked assets. However, the use of a fair value accounting policy for such liabilities is not explicitly permitted by Schedule 9A.

In practice the use of an amortised cost measurement basis may achieve the same result. Paragraph 22 of the ASB's Guidance on the 'Carved out' IAS 39 states that "it is not always necessary to measure a financial liability at fair value through profit or loss in order to measure a liability that is contractually linked to changes in value of one or more assets at an amount that reflects the value of the linked assets. That is because, for those linked liabilities where the counterparty has the contractual right to demand payment of the liability at any time without penalty, the amortised cost of a linked liability could be viewed as the amount payable. Thus applying a cost basis may also result in the liability being measured at an amount that reflects the value of the linked asset."

If the amortised cost policy is adopted for unit-linked financial liabilities, and disclosed accordingly, then the required matching of the liabilities to the related assets may be achieved without any need for a true and fair override. This is the policy adopted by Proforma-Life Limited for the measurement of unit-linked investment contract liabilities.

Where financial liabilities are valued at amortised cost (as opposed to at fair value through profit and loss) there is no exemption from the requirement to separate embedded derivatives that are not closely related to the host contract.

Non unit-linked non-profit investment contracts

PwC

For non unit-linked non-profit investment contracts, the measurement of financial liabilities at amortised cost may give rise to a potential for substantial artificial volatility being introduced (for example, where the assets would be revalued as market interest rates moved but the corresponding financial liabilities would not). In these circumstances it is likely that companies would need to use a true and fair override of the provisions of the Companies Act in order to measure such liabilities at fair value. In circumstances where the measurement of liabilities at amortised cost would not give rise to a potential for substantial artificial volatility there would not appear to be justification for using a true and fair override and such liabilities should be measured at amortised cost.

Proforma-Life Limited has no non unit-linked non-profit investment contracts.

Deferred origination costs

ABI, 161

Incremental costs that are directly attributable to securing an investment management contract (such as the unit-linked contracts recognised by Proforma-Life Limited as investment contracts under FRS 26) are recognised as a deferred acquisition costs asset if they can be identified separately and measured reliably and if it is probable that they will be recovered. An incremental cost is one that would not have been incurred if the entity had not secured the investment management contract. The asset represents the entity's contractual right to benefit from providing investment management services and is amortised as the entity recognises the related revenue. If the entity has a portfolio of investment management contracts, it may assess their recoverability on a portfolio basis.

G. Investment return

ABI, 44, 288

Investment return comprises all investment income (which includes the interest income for financial assets carried at amortised cost, using the effective interest method), realised investment gains and losses and movements in unrealised gains and losses, net of investment expenses, charges and interest payable on financial liabilities carried at amortised cost, using the effective interest method.

ABI, 310

Dividends are included as investment income on the date that the shares are quoted ex-dividend and include the imputed tax credits. Interest, rent and expenses are accounted for on an accruals basis.

FRS 29, 21B

Realised gains and losses on investments carried at fair value are calculated as the difference between net sales proceeds and purchase price. In the case of investments included at amortised cost, realised gains and losses are calculated as the difference between sale proceeds and their latest carrying value. Movements in unrealised gains and losses on investments represent the difference between the fair value at the balance sheet date and their purchase price or their fair value at the last balance sheet date, together with the reversal of unrealised gains and losses recognised in earlier accounting periods in respect of investment disposals in the current period.

FRS 29, 21B

An entity is required to disclose the basis for reporting realised and unrealised gains and losses, interest and other items of income and expense associated with financial assets and financial liabilities.

Calculation of realised investment gains

FRS 3, 31A

Insurance companies are exempt from the general requirement of FRS 3 to measure 'realised gains' by reference to the net carrying amount.

ABI, 286, 287

Investment return relating to investments which are directly connected with the carrying on of long-term business is initially recorded in the long-term business technical account. The investment return arising in relation to all other investments is recorded in the non-technical account. An allocation of investment return is made from the long-term business technical account to the non-technical account in order that investment return retained and reported in the technical account on investments directly attributable to shareholders reflects the directors' estimate of the longer-term rate of return. The allocation is made gross of any attributable tax.

ABI, 48

The longer-term rate of investment return is an estimate of the long-term trend investment return for the relevant category of investments having regard to past performance, current trends and future expectations.

ABI, 291

The ABI SORP permits, but does not require, a form of presentation which enables the reader to identify operating results based on the longer term rate of investment return. This return may be recorded within the long-term business technical account and may also be disclosed separately as part of the total operating profit.

ABI, 286

The ABI SORP defines investments directly connected with the carrying on of long-term business as those investments arising in, or attributed to, the long-term fund, including the fund for future appropriations, together with such directly connected investments where the return accrues to shareholders whether held within or outside the long-term business fund.

ABI, 295

The ABI SORP defines investments directly attributable to shareholders as those supporting the long-term business other than assets supporting (i) the long-term business provision, (ii) the fund for future appropriations; and (iii) the technical provisions for linked liabilities. This is the treatment adopted in the Proforma-Life Limited accounts. Alternatively, disclosure of technical results reflecting the longer-term rate of return may be made as a memorandum item on the face of the profit and loss account without making any actual allocation of investment return.

ABI, 298

Where an allocation of return is made, the allocation to the non-technical account is required to be gross of any tax. In order to do this the tax attributable to the allocated investment return is deducted from the tax attributable to the long-term business (technical account item II.11A) and added to the tax on profit or loss on ordinary activities (non-technical account item III.9).

ABI, 293

In the case of an insurance company or group transacting both general and long-term insurance business, the ABI SORP requires consistency of treatment in the allocation of investment return. Hence, where the longer-term rate basis of allocation is used, it must be applied to both the general and the long-term insurance business. Where an allocation of actual investment return is made from the non-technical account to the general business technical account in respect of investments supporting the general business technical provisions and associated shareholders' funds, no allocation of return should be made from the long-term business technical account to the non-technical account.

H. Goodwill

FRS 10, 55
Sch9A, 36

Goodwill is capitalised in the balance sheet at cost and amortised through the profit and loss account on a straight line basis over its useful economic life. Goodwill is tested annually for impairment. The gain or loss on subsequent disposal of a subsidiary or associated undertaking will include any attributable unamortised goodwill.

FRS 10, 71(a)

Prior to 1998, purchased goodwill was eliminated against reserves as a matter of accounting policy. As permitted under the transitional arrangements of FRS 10, such amounts previously written off to reserves have not been reinstated as an asset, but will be charged to the profit and loss account on any disposal of the business to which they relate.

FRS 10, 7&8

FRS 10 'Goodwill and intangible assets' requires purchased goodwill to be capitalised as an asset in the balance sheet. Internally generated goodwill should not be capitalised.

FRS 10, 15, 55, 58, 59

Where goodwill is regarded as being of limited economic life it should be amortised over that life. The methods and periods of amortisation adopted should be disclosed. There is a rebuttable presumption that the purchased goodwill has a finite useful economic life of less than 20 years. Additional disclosures are required if goodwill is either not amortised, or amortised over a period of more than 20 years.

FRS 10, 34

The carrying value of goodwill being amortised over a period of 20 years or less needs to be reviewed for impairment at the end of the first full financial year following the initial recognition of the goodwill and subsequently only when events or changes in circumstances indicate the goodwill may not be recoverable in full.

FRS 10, 69

Transitional provisions allowed goodwill previously written off against reserves to be reinstated on the first application of FRS 10. This option could have been exercised in respect of:

- goodwill relating to acquisitions made before 23 December 1989 (where the information is not readily available without unreasonable expense or delay);
- goodwill eliminated prior to implementation of FRS 7; or
- all goodwill previously eliminated.

FRS 10, 71

Where the transitional provisions have been utilised, disclosure is required of the accounting policy adopted, the amount of goodwill remaining eliminated against reserves and the fact that this will be charged to the profit and loss account on a subsequent disposal. On first application of FRS 10, Proforma-Life Limited adopted the transitional provisions in respect of all goodwill previously eliminated.

UITF 27, 5

Where estimates of the useful economic lives of goodwill or intangible assets are revised, the carrying value should be amortised over the revised remaining useful economic life. This requirement applies equally where the presumption of a 20-year life has previously been rebutted as it does to other revisions of estimates of the useful economic lives of goodwill and intangible assets.

I. Investments

Land and buildings

Sch9A, 22(1), 26, 28(2)

Land and buildings are valued at open market valuation. Full valuations are made by independent, professionally qualified valuers every three years. In the intervening years these valuations are updated by the directors with the assistance of independent professional advice as required.

Sch9A, 32
SSAP 19
FRS 18, 62

In accordance with SSAP 19, no depreciation or amortisation is provided in respect of freehold investment properties and leasehold investment properties with over 20 years to run. The requirement of the Companies Act 1985 is to depreciate all properties. This requirement conflicts with the generally accepted accounting principle set out in SSAP 19. The directors consider that, as these properties are held for investment, to depreciate them would not give a true and fair view, and that it is necessary to adopt SSAP 19 in order to give a true and fair view. Depreciation is only one of the factors reflected in the annual valuations, and the amounts which might otherwise have been shown cannot reasonably be separately identified or quantified.

ABI, 267

Owner-occupied properties do not satisfy the definition of investment properties and so are not exempt from the requirement that they are depreciated. In the accounts of Proforma-Life Limited, such depreciation would be immaterial.

Investments in Group undertakings and participating interests

In the balance sheet of the Company, investments in Group undertakings and participating interests are stated at cost, unless their value has been impaired, in which case they are valued at their realisable value or value in use as appropriate. Participating interests are included in the consolidated balance sheet at the Group's share of their net assets.

ABI, 269, 34, 273

In single entity insurance company accounts, shares in group undertakings and participating interests are required to be stated at current value, determined in accordance with paragraph 25 of Schedule 9A of the Companies Act 1985, which requires insurers to have prudent regard to the likely realisable value when valuing unlisted investments.

Sch4, 31
ABI, 278

Movements in the value of investments in group undertakings and participating interests shown in the balance sheet at current value and not attributable to the long-term business should be taken to revaluation reserve. Valuation movements on interests attributable to the long-term business should be taken to the long-term business technical account. Proforma-Life Limited is a non-insurance holding company preparing entity accounts in accordance with Schedule 4. Under Schedule 4 investments may be included at historical cost, market value or any basis which appears to the directors to be appropriate. FRS 26 does not apply to those interests in subsidiary, quasi-subsidiary and associated undertakings, partnerships and joint ventures that are accounted for under FRS 2 'Accounting for subsidiary undertakings'; FRS 5 'Reporting the substance of transactions'; and FRS 9 'Associates and joint ventures', unless held for resale. FRS 26 will however apply to derivatives on an interest in a subsidiary, quasi-subsidiary or associated undertaking, partnership or joint venture unless the derivative meets the definition of an equity instrument of the entity under FRS 25.

FRS 25 'Financial instruments: Presentation', FRS 26 'Financial instruments: Recognition and Measurement' and FRS 29 'Financial instruments: Disclosures'

FRS 25 and FRS 26 implement IAS 32 and IAS 39 respectively into UK GAAP. FRS 26 sets out the requirements for the recognition and measurement of financial instruments whereas FRS 25 addresses the presentation requirements. The application of FRS 26 is mandatory for listed entities and unlisted entities applying the Companies Act 1985 fair value accounting rules or marking to market any financial instrument that (in the case of insurers) is not explicitly permitted by Schedule 9A. In practice any unlisted insurer that holds any derivatives at fair value is within the scope of FRS 26 (and also FRSs 23, 24 and 29).

The presentation requirements of FRS 25 (which dealt with issues such as the presentation of preference shares as liabilities as opposed to equity) apply to all entities.

FRS 29, 43, 44 Disclosure provisions in respect of financial instruments are set out in FRS 29 'Financial instruments: Disclosures' (which implements IFRS 7 into UK GAAP).

Recognition and derecognition

FRS 26 incorporates the provisions of IAS 39 relating to recognition and derecognition of financial instruments. FRS 5 and the ABI SORP continue to apply to the recognition and derecognition of non-financial assets and liabilities.

FRS 26, 14 An entity only recognises a financial asset or liability at the time it becomes a party to the instrument's contractual provisions i.e. at the time it has the contractual rights or obligations.

PwC Recognition issues for financial assets and liabilities tend to be straightforward whereas derecognition issues , particularly in relation to financial assets, can be complex. Many financial instruments comprise components – bundles of contractual rights and/or contractual obligations that are financial assets and financial liabilities in their own right. Transactions may occur that leave in place certain of the components that give rights to future benefits, while transferring the other components to one or more parties. Securitisation transactions, loan transfers and transfers involving derivatives, debt factoring, repurchase agreements and stock lending agreements are examples of such complex transactions.

FRS 26, 38 A 'regular way' purchase of securities may be recognised using either trade date or settlement date accounting, providing the method is applied consistently within each of the four categories of financial assets.

FRS 26, 9 FRS 26 defines a regular way purchase (or sale) of securities as a contract whose terms require delivery of the asset within the time frame established generally by regulation or convention in the marketplace concerned. A contract that requires or permits net settlement of the change in the value of the contract is not a regular way contract. Instead, such a contract is accounted for as a derivative in the period between the trade date and the settlement date.

FRS 26, 15-23 Derecognition of a financial asset occurs only when the seller has transferred the asset's risks and rewards (either substantially or partially) or control of the contractual rights have been transferred from the seller to the buyer. The evaluation of the transfer of risks and rewards should precede an evaluation of the transfer of control for all types of transaction. The positions of both the buyer and the seller should be considered but the seller's position is seen as more relevant. An entity may achieve partial derecognition whereby it recognises the components that have been retained, or new assets or liabilities such as those that arise from issuing a guarantee.

PwC Even though legal transfer may have occurred, this does not necessarily lead to the derecognition of a financial asset if risks and rewards of the asset are retained.

FRS 26, AG36

FRS 26 acknowledges the complexity of the derecognition provisions in relation to financial assets and introduces a step-by-step approach to analysing transactions that sets out when and in what order the various approaches are to be applied. A flowchart is provided to assist in evaluating whether and to what extent a financial asset is derecognised.

FRS 26, 26

On derecognition, the difference between the amount received and the asset's carrying amount is recognised in profit or loss. Any fair value adjustment to the asset formerly reported in equity is recycled to profit or loss.

FRS 26, 39

The derecognition rules for financial liabilities focus solely on the legal release of the contractual obligations.

FRS 26, 41

On derecognition, the difference between the consideration paid and the liability's carrying amount is recognised in profit or loss.

Initial measurement

FRS 26, 43

When a financial asset (or liability) is recognised initially, an entity shall measure it at its fair value plus, in the case of a financial asset (or liability) not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the financial asset or liability.

FRS 26, AG64
FRS 29, 28

The best evidence of fair value at initial recognition is the transaction price (i.e. the fair value of the consideration given or received). However for financial instruments for which there is no active market there could be a difference between the fair value at initial recognition and the amount that would be determined at that date using the valuation technique. If such a difference exists, an entity shall disclose, by class of financial instrument:

(a) its accounting policy for recognising that difference in profit or loss to reflect a change in factors (including time) that market participants would consider in setting a price; and
(b) the aggregate difference yet to be recognised in profit or loss at the beginning and end of the period and a reconciliation of changes in the balance of this difference.

FRS 26, AG64

If part of the consideration given or received is for something other than the financial instrument, the fair value of the financial instrument is estimated, using a valuation technique. For example, the fair value of a long-term loan or receivable that carries no interest can be estimated as the present value of all future cash receipts discounted using the prevailing market rate(s) of interest for a similar instrument (similar as to currency, term, type of interest rate and other factors) with a similar credit rating. Any additional amount lent is an expense or a reduction of income unless it qualifies for recognition as some other type of asset.

Subsequent measurement

FRS 26, 46

After initial recognition, an entity shall measure financial assets, including derivatives that are assets, at their fair values, without any deduction for transaction costs it may incur on sale or other disposal, except for the following financial assets:

(a) loans and receivables shall be measured at amortised cost using the effective interest method;
(b) held-to-maturity investments shall be measured at amortised cost using the effective interest method; and
(c) investments in equity instruments that do not have a quoted market price in an active market and whose fair value cannot be reliably measured and derivatives that are linked to and must be settled by delivery of such unquoted equity instruments, shall be measured at cost.

All financial assets except those measured at fair value through profit or loss are subject to review for impairment.

Fair value option

FRS 26, 9, 55 Under FRS 26 financial assets that are measured at fair value are either accounted for at fair value through profit and loss (where all gains and losses are taken to the profit and loss account) or as available for sale (AFS) where unrealised gains and losses (other than impairment losses) are initially recorded in the statement of total recognised gains and losses.

FRS 26, 9 Financial assets that are held for trading (including all derivatives) are required to be accounted for at fair value through profit and loss.

FRS 26, 9 Other financial assets measured at fair value will be accounted for as AFS unless they are designated as at fair value through profit and loss. A financial asset may be so designated where doing so results in more relevant information, because either:

- it eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as 'an accounting mismatch') that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases; or
- a group of financial assets, financial liabilities or both is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, and information about the group is provided internally on that basis to the entity's key management personnel, for example the entity's board of directors and chief executive officer.

Amortised cost

FRS 26, 9 The amortised cost is the amount at which the financial asset, or financial liability, is measured at initial recognition minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount, and minus any reduction (directly or through the use of an allowance account) for impairment or uncollectibility.

Effective interest method

FRS 26, 9 The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability (or group of financial assets or financial liabilities) and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, an entity shall estimate cash flows considering all contractual terms of the financial instrument (for example, prepayment, call and similar options) but shall not consider future credit losses. In those rare cases when it is not possible to estimate reliably the cash flows or the expected life of a financial instrument (or group of financial instruments), the entity shall use the contractual cash flows over the full contractual term of the financial instrument (or group of financial instruments).

FRS 26, AG 6 When applying the effective interest method, an entity generally amortises any fees, points paid or received, transaction costs and other premiums or discounts included in the calculation of the effective interest rate over the expected life of the instrument. However, a shorter period is used if this is the period to which the fees, points paid or received, transaction costs, premiums or discounts relate.

FRS 26, AG 7 For floating rate financial assets and floating rate financial liabilities, periodic re-estimation of cash flows to reflect movements in market rates of interest alters the effective interest rate. If a floating rate financial asset or floating rate financial liability is recognised initially at an amount equal to the principal receivable or payable on maturity, re-estimating the future interest payments normally has no significant effect on the carrying amount of the asset or liability.

FRS 26, AG 8 If an entity revises its estimates of payments or receipts, the entity shall adjust the carrying amount of the financial asset or financial liability (or group of financial instruments) to reflect actual and revised estimated cash flows. The entity recalculates the carrying amount by computing the present value of estimated future cash flows at the financial instrument's original effective interest rate. The adjustment is recognised as income or expense in profit or loss.

Reclassification of certain financial assets – amendment to FRS 26

FRS 26, 50B, 50D

In October 2008 the IASB issued amendments to IAS39, 'Financial instruments: Recognition and measurement' and IFRS7, 'Financial instruments: Disclosures', that permit the reclassification of some financial assets.
From 1 July 2008, reclassifications of financial assets classified as held for trading (but not designated under the fair value option), are permitted:

- if the financial asset meets the definition of a loan or receivable at the date of reclassification and the entity now has the intent and ability to hold it for the foreseeable future or to maturity; and
- for other financial assets (that is, those that do not meet the definition of a loan or receivable at the date of reclassification), the financial asset may be reclassified only in rare circumstances.

From 1 July 2008, assets classified as available-for-sale (AFS) may be reclassified as loans and receivables provided:

- they would have met the definition of a loan or receivable, and
- the company has the intent and ability to hold the asset for the foreseeable future or to maturity.

FRS26, 103G

Any reclassification made on or after 1 November 2008 takes effect from the date of reclassification. However, any reclassification before 1 November 2008 could take effect from 1 July 2008 or a subsequent date. A reclassification cannot be applied retrospectively before 1 July 2008.

FRS26, 50F

At the date of reclassification the fair value of any financial asset reclassified under these provisions becomes its new cost or amortised cost as applicable. The entity will spread over the life of the asset the effect of any subsequent increase in the estimated cash receipts of a reclassified asset as a result of increased recoverability of those cash receipts by adjusting the effective interest rate prospectively, rather than recognising the impact of the increasing cash receipts immediately in the profit or loss account under the cumulative catch-up approach in FRS 26.

Proforma-Life has not reclassified any financial assets under the amendments to FRS 26.

Fair value measurement considerations

In determining the fair value of a financial asset (or liability) for the purposes of FRS 26 the following applies:

(i) Active market: quoted price

FRS 26, AG 71, AG 72

A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis. The appropriate quoted market price for an asset held is usually the current bid price. When current bid prices are unavailable, the price of the most recent transaction provides evidence of the current fair value as long as there has not been a significant change in economic circumstances since the time of the transaction. If conditions have changed since the time of the transaction, the fair value reflects the change in conditions by reference to current prices or rates for similar financial instruments, as appropriate.

(ii) No active market: valuation technique

FRS 26, AG 74

If the market for a financial instrument is not active, an entity establishes fair value by using a valuation technique. Valuation techniques include using recent arm's length market transactions between knowledgeable, willing parties, if available; reference to the current fair value of another instrument that is substantially the same; discounted cash flow analysis; and option pricing models. If there is a valuation technique commonly used by market participants to price the instrument and that technique has been demonstrated to provide reliable estimates of prices obtained in actual market transactions, the entity uses that technique.

(iii) No active market: equity instruments

FRS 26, AG 80-81

The fair value of investments in equity instruments that do not have a quoted market price in an active market and derivatives that are linked to and must be settled by delivery of such an unquoted equity instrument is reliably measurable if (a) the variability in the range of reasonable fair value estimates is not significant for that instrument; or (b) the probabilities of the various estimates within the range can be reasonably assessed and used in estimating fair value. If a reasonable assessment cannot be made then the instrument cannot be carried at fair value.

IASB – Guidance on Applying fair value in inactive markets

In October 2008 the IASB issued educational guidance: 'Measuring and disclosing the fair value of financial instruments in markets that are no longer active'. The guidance is in partly a response to the concerns raised by the Financial Stability Forum report issued back in April 2008. The report provides guidance about the processes used and the judgements made when measuring and disclosing fair value.

Disclosure of accounting policies

An insurer is required to include the following within its accounting policy for financial instruments:

- basis of recognition and measurement of financial assets (cost or valuation);
- FRS 26, 45 — basis of classification of financial assets between classes (see also Note 20 'Other financial investments');
- FRS 29, 43-44 — methods and, where a valuation technique is used, assumptions applied in determining fair values for each class of financial assets or financial liabilities;
- FRS 26, 58 — recognition and measurement of impairment of financial assets;
- FRS 29, App B5 (a) — for financial assets designated as at fair value through profit or loss:
  - (i) the nature of the financial assets or financial liabilities the entity has designated as at fair value through profit or loss;
  - (ii) the criteria for so designating such financial assets or financial liabilities on initial recognition; and
  - (iii) how the entity has satisfied the FRS 26 conditions for such designation. Narrative descriptions may be required to explain either (i) the circumstances underlying the measurement or recognition inconsistency that would otherwise arise if this designation was not used; or (ii) how this designation is consistent with the entity's documented risk management or investment strategy;
- FRS 29, App B5 (b) — the criteria for designating financial assets as available for sale;
- FRS 29, App B5 (d) — when an allowance account is used to reduce the carrying amount of financial assets impaired by credit losses:
  - (i) the criteria for determining when the carrying amount of impaired financial assets is reduced directly (or, in the case of a reversal of a write-down, increased directly) and when the allowance account is used; and
  - (ii) the criteria for writing off amounts charged to the allowance account against the carrying amount of impaired financial assets;
- FRS 29, App B5 (e) — how net gains or net losses on each category of financial instruments are determined;
- FRS 29, App B5 (f) — the criteria the entity uses to determine that there is objective evidence that an impairment loss has occurred; and
- FRS 29, App B5 (g) — when the terms of financial assets that would otherwise be past due or impaired have been re-negotiated, the accounting policy for financial assets that are the subject of re-negotiated terms.

FRS 29, 4

FRS 29 applies to recognised and unrecognised financial instruments. Recognised financial instruments include financial assets and financial liabilities that are within the scope of FRS 26. Unrecognised financial instruments include some financial instruments that, although outside the scope of FRS 26, are within the scope of FRS 29 (such as some loan commitments).

FRS 29, 6,B2, B3

Certain disclosures are required by class of financial instrument, which are determined by the entity and are, thus, distinct from the categories of financial instruments specified in FRS 26. Financial instruments should be grouped into classes that are appropriate to the nature of the information disclosed and that take into account the characteristics of those financial instruments. Sufficient information should be provided to permit reconciliation to the line items presented in the balance sheet. As a minimum an entity shall distinguish between instruments measured at amortised cost from those measured at fair value and treat any financial instruments outside the scope of FRS 26 as a separate class. The objective of this exercise is to combine information so as to display the overall picture without combining information with different characteristics. It is necessary to strike a balance between excessive detail and obscuring important information.

FRS29p12, 12A

In October 2008 FRS 29 was amended to incorporate extensive disclosure requirements relating to any assets reclassified as a result of the amendment to FRS 26. In particular, an entity is required to disclose details of carrying amounts and fair values for all financial assets that have been reclassified until they are derecognised, together with details of the fair value gain or loss that would have been recognised in the income statement or equity if the financial asset had not been reclassified.

FRS 29, 2D

Subsidiary undertakings, other than banks or insurance companies, 90% or more of whose voting rights are controlled within the group, are exempt from FRS 29 provided the entity is included in publicly available consolidated financial statements which include FRS 29 disclosures.

This exemption also includes parent companies in respect of their single-entity financial statements. As a result in the consolidated financial statements, FRS 29 disclosures are only required at the group level.

Other financial investments

FRS 26, 9

The Group classifies its financial assets into the following categories: Shares and other variable-yield securities and units in unit trusts – at fair value through profit or loss; Debt securities and other fixed-income securities – at fair value through profit or loss; Debt securities and other fixed-income securities - held to maturity (where there is a positive intention to hold to maturity) or, otherwise, at fair value through profit or loss; and Deposits with credit institutions - loans and receivables. Management determines the classification of its investments at initial recognition and re-evaluates this at every reporting date.

(a) Shares and other variable-yield securities and units in unit trusts, and debt securities and other fixed interest securities – at fair value through profit or loss

A financial asset is classified into this category at inception if they are acquired principally for the purpose of selling in the short term, if they form part of a portfolio of financial assets in which there is evidence of short-term profit-taking, or if so designated by management to minimise any measurement or recognition inconsistency with the associated liabilities.

Financial assets designated as at fair value through profit and loss at inception are those that are managed and whose performance is evaluated on a fair value basis. Information about these financial assets is provided internally on a fair value basis to the Group entity's key management personnel. The Group's investment strategy is to invest in listed and unlisted equity securities and fixed interest rate debt securities, and derivatives designated upon initial recognition at fair value through profit or loss.

FRS 26, AG 70
Sch9A, 25

The fair values of listed investments are based on current bid prices on the balance sheet date. Unlisted investments for which a market exists are also stated at the current bid price on the balance sheet date or the last trading day before that date. The fair values of other unlisted investments, for which no active market exists, are established by the directors using valuation techniques which have prudent regard to the likely realisable value. These include use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis and other pricing models having regard to the valuation guidelines given by the British Venture Capital Association, the European Private Equity and Venture Capital Association and the Association Française des Investisseurs en Capital.

Sch9A, 65A(4)

Net gains or losses arising from changes in the fair value of financial assets at fair value through profit or loss are presented in the profit and loss account within 'Unrealised gains on investments' or 'Unrealised losses on investments' in the period in which they arise.

(b) Debt securities and other fixed-income securities - held to maturity

FRS 26, 9

Redeemable fixed interest securities, in respect of which there is a positive intention to hold to maturity are valued at amortised cost. The amortisation is calculated so as to write off the difference between the purchase price and the maturity value over the life of the security, using the effective interest method.

Alternative valuation of fixed income securities

Sch9A, 24

Schedule 9A provides the option that debt and other fixed income securities may be included in the balance sheet at amortised cost rather than current value.

FRS 26, 9
ABI, 279

Under FRS 26 the 'held-to-maturity' heading for investments comprises non-derivative financial assets with fixed and determinable payments and fixed maturity that an entity has the positive intention and ability to hold to maturity. This is a stricter requirement than that which applies to insurers not adopting FRS 26 who can use amortised cost for redeemable fixed interest securities for any part of a portfolio intended to be held on an ongoing basis.

FRS 26, 9

An entity shall not classify any financial assets as held to maturity if the entity has, during the current financial year or during the two preceding financial years, sold or reclassified more than an insignificant amount of held-to-maturity investments before maturity (more than insignificant in relation to the total amount of held-to-maturity investments) other than sales or reclassifications that:

(i) are so close to maturity or the financial asset's call date (for example, less than three months before maturity) that changes in the market rate of interest would not have a significant effect on the financial asset's fair value;
(ii) occur after the entity has collected substantially all of the financial asset's original principal through scheduled payments or prepayments; or
(iii) are attributable to an isolated event that is beyond the entity's control, is non-recurring and could not have been reasonably anticipated by the entity.

For illustrative purposes, Proforma-Life Limited has met the necessary requirements of FRS 26 to enable certain debt securities and other fixed-income securities to be classified as "held-to-maturity".

(c) Deposits with credit institutions - Loans and receivables

FRS 26, 9

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market other than those that the Group intends to sell in the short term or that it has designated as at fair value through profit or loss. When a financial asset is recognised initially it is measured at fair value plus transaction costs that are directly attributable to the acquisition or issue of the financial asset. Loans and receivables are subsequently measured at amortised cost using the effective interest method. Receivables arising from insurance contracts are also classified in this category and are reviewed for impairment as part of the impairment review of loans and receivables. This basis of valuation is viewed by the directors as having prudent regard to the likely realisable value.

Sch9A, 25(5)

Sch9A, 24(1)
Sch9A, 25(5)

The Schedule 9A rules in respect of investments at amortised cost only apply to debt securities and other fixed-income securities. To the extent that a company values other loans and receivables at amortised cost under the provisions of FRS 26 then such a basis will need to represent "a basis which has prudent regard to the likely realisable value" in accordance with the current value accounting rules.

J. Impairment of financial assets

FRS 26, 58, 61

For financial assets not at fair value through profit and loss, the Group assesses at each balance sheet date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that have occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. Objective evidence that a financial asset or group of assets is impaired includes observable data that comes to the attention of the Group about the following events:

FRS 26, 59

(a) significant financial difficulty of the issuer or debtor;

(b) a breach of contract, such as a default or delinquency in payments;

(c) it becoming probable that the issuer or debtor will enter bankruptcy or other financial reorganisation;

(d) the disappearance of an active market for that financial asset because of financial difficulties; or

(e) observable data indicating that there is a measurable decrease in the estimated future cash flow from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the group, including:

- adverse changes in the payment status of issuers or debtors in the group; or
- national or local economic conditions that correlate with defaults on the assets in the group.

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss has been incurred on loans and receivables or held-to-maturity investments carried at amortised cost, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced and the amount of the loss is recognised in the profit and loss account for the period. If a held-to-maturity investment or a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under contract. As a practical expedient, the Group may measure impairment on the basis of an instrument's fair value using an observable market price.

For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics (i.e. on the basis of the Group's grading process that considers asset type, industry, geographical location, past-due status and other relevant factors). Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the issuer's ability to pay all amounts due under the contractual terms of the debt instrument being evaluated.

If in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as improved credit rating), the previously recognised impairment loss is reversed through the profit and loss account for the period.

Impairment of financial assets

FRS 26, 63 *Financial assets at amortised cost*

FRS 26 permits an entity to account for impairment losses on financial assets held at amortised cost by either reducing the carrying amount of the asset directly or through the use of an allowance account.

Financial assets carried at cost

FRS 26, 66 If there is objective evidence that an impairment loss has been incurred on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured, or on a derivative asset that is linked to and must be settled by delivery of such an unquoted equity instrument, the amount of the impairment loss is measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset. Such impairment losses shall not be reversed.

FRS 29, 20(e) The amount of any impairment loss for each class of financial asset should be disclosed. Proforma-Life Limited has no impairment losses.

FRS 29, 16 Where an allowance account is used to record individual impairments, a reconciliation of the changes in that account during the period for each class of financial assets should be disclosed.

Available for sale financial assets

FRS 29, 67
FRS 29, 69 Where there is objective evidence of impairment of available for sale financial (AFS) assets the cumulative loss that had been recognised directly in equity is removed from equity and charged to profit and loss. The impairment loss is calculated as the difference between the acquisition cost (net of any principal repayment and amortisation) and current fair value (less previously recognised impairment).

FRS 29, 61 For AFS equities a significant or prolonged decline in fair value below cost is objective evidence of impairment.

FRS 29, 69
FRS 29, 70 Impairment losses on AFS equities cannot be reversed through income. Impairment losses on AFS debt securities can be reversed if, in a subsequent period, the fair value of the instrument increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss.

Proforma-Life Limited has no available for sale financial assets.

K. Derivative financial instruments

FRS 26, 43, 46 Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently re-measured at their fair value. Changes in the fair value are recognised immediately in the profit and loss account. Fair values are obtained from quoted market prices in active markets, including recent market transactions, and valuation techniques, including discounted cash flow models and options pricing models, as appropriate. All derivatives are carried as assets when the fair value is positive and as liabilities when the fair value is negative.

FRS 26, AG 64 The best evidence of the fair value of a derivative at initial recognition is the transaction price (i.e. the fair value of the consideration given or received) unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets.

When unobservable market data has an impact on the valuation of derivatives, the entire initial change in fair value indicated by the valuation model is not recognised immediately in the profit and loss account but is recognised over the life of the transaction on an appropriate basis or is recognised in the profit and loss account when the inputs become observable, or when the transaction matures or is closed out.

FRS 26, 10, 11 Embedded derivatives that are not closely related to their host contracts and meet the definition of a derivative are separated and fair valued through the profit and loss account.

FRS 26 (IAS 39) ‘Financial instruments: Recognition and Measurement’

Hedging

FRS 26, 71 If there is a designated hedging relationship between a hedging instrument (which in most circumstances will be a derivative) and a hedged item, accounting for the gain or loss on the hedging instrument and the hedged item will follow the treatments set out in FRS 26.

FRS 26, 86 Hedging relationships are of three types:

FRS 26, 29 (i) fair value hedges (where the gain or loss on the hedging instrument and gains or losses on the hedged item arising from the hedged risk are recognised in profit or loss);

FRS 26, 95 (ii) cash flow hedges (where the gain or loss on the effective portion of the hedging instrument is taken through the statement of total recognised gains and losses until the hedged transaction affects the profit and loss account); or

FRS 26, 102 (iii) hedges of a net investment in a foreign operation (where the gain or loss on the effective portion of the hedging instrument is taken through the statement of total recognised gains and losses to match the gain or loss on net assets).

Qualifying hedges

FRS 26, 73 For hedge accounting purposes, only instruments that involve a party external to the reporting entity (i.e. external to the group, segment or individual entity that is being reported on) can be designated as hedging instruments. Although individual entities within a consolidated group or divisions within an entity may enter into hedging transactions with other entities within the group or divisions within the entity, any such intragroup transactions are eliminated on consolidation. Therefore, such hedging transactions do not qualify for hedge accounting in the consolidated financial statements of the group. However they may qualify for hedge accounting in the individual or separate financial statements of individual entities within the group or in segment reporting provided that they are external to the individual entity or segment that is being reported on.

FRS 26, 88 A hedge relationship qualifies for hedge accounting if, and only if, all of the following conditions are met:

- at the inception of the hedge there is a formal designation and documentation of the hedging relationship and the entity’s risk management objective and strategy for undertaking the hedge. That documentation shall include identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the entity will assess the hedging instrument’s effectiveness in offsetting the exposure to changes in the hedged item’s fair value or cash flows attributable to the hedged risk;
- the hedge is expected to be highly effective in achieving offsetting changes in fair value or cash flows attributable to the hedged risk, consistently with the originally documented risk management strategy for that particular hedging relationship;
- for cash flow hedges, a forecast transaction that is the subject of the hedge must be highly probable and must present an exposure to variations in cash flows that could ultimately affect profit or loss;
- the effectiveness of the hedge can be reliably measured; and
- the hedge is assessed on an ongoing basis and determined actually to have been highly effective throughout the financial reporting periods for which the hedge was designated.

Disclosure of hedging transactions

FRS 29, 22 For each type of hedging relationship the following should be disclosed:

(a) a description of each type of hedge;

(b) a description of the financial instruments designated as hedging instruments and their fair values at the reporting date; and

(c) the nature of the risks being hedged.

FRS 29, 23

The following additional disclosures are required for cash flow hedges:

(a) the periods when the cash flows are expected to occur and when they are expected to affect profit or loss;

(b) a description of any forecast transaction for which hedge accounting had previously been used, but which is no longer expected to occur;

(c) the amount that was recognised in equity during the period;

(d) the amount that was removed from equity and included in profit or loss for the period, showing the amount included in each line item in the income statement; and

(e) the amount that was removed from equity during the period and included in the initial cost or other carrying amount of a non-financial asset or non-financial liability whose acquisition or incurrence was a hedged highly probable forecast transaction.

FRS 29, 24

The impact of hedging transactions on profit or loss are required as follows:

(a) in fair value hedges, gains or losses:
   (i) on the hedging instrument; and
   (ii) on the hedged item attributable to the hedged risk;

(b) the ineffectiveness recognised in profit or loss that arises from cash flow hedges; and

(c) the ineffectiveness recognised in profit or loss that arises from hedges of net investments in foreign operations.

Proforma-Life Limited has no designated hedging relationships.

Embedded derivatives

FRS 26, 10

An embedded derivative is a component of a hybrid (combined) instrument that also includes a non-derivative host contract.

FRS 26,11

An embedded derivative shall be separated from the host contract and accounted for as a derivative under FRS 26 if, and only if:

(a) the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract;

(b) a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative; and

FRS 26, 2(e)

(c) the hybrid (combined) instrument is not measured at fair value with changes in fair value recognised in profit or loss (i.e. a derivative that is embedded in a financial asset or financial liability at fair value through profit or loss is not separated).The above requirements apply to derivatives embedded in an insurance contract unless the embedded derivative is itself an insurance contract.

FRS 26, 11

If an embedded derivative is separated, the host contract shall be accounted for under FRS 26 if it is a financial instrument and in accordance with other appropriate standards if it is not a financial instrument.

FRS 26, 11A

Notwithstanding the above, if a contract contains one or more embedded derivatives, an entity may designate the entire hybrid (combined) contract as a financial asset or financial liability at fair value through profit or loss unless:

(a) the embedded derivative(s) does not significantly modify the cash flows that otherwise would be required by the contract; or

(b) it is clear with little or no analysis when a similar hybrid (combined) instrument is first considered that separation of the embedded derivative(s) is prohibited, such as a prepayment option embedded in a loan that permits the holder to prepay the loan for approximately its amortised cost.

FRS 26, 12

If an entity is required to separate an embedded derivative from its host contract, but is unable to measure the embedded derivative separately either at acquisition or at a subsequent financial reporting date, it shall designate the entire hybrid (combined) contract as at fair value through profit or loss.

FRS 29, 17

If an instrument contains both a liability and an equity component under FRS 25 and the instrument has multiple embedded derivatives whose values are interdependent, those features should be disclosed.

Proforma-Life Limited has no embedded derivatives that require separation.

L. Present value of acquired in-force business

ABI, 58

On acquisition of a portfolio of long-term insurance contracts, either directly or through the acquisition of a subsidiary undertaking, the net present value of the shareholders' interest in the expected after-tax cash-flows of the in-force business is capitalised in the balance sheet as an asset. That part of the shareholders' interest which will be recognised as profit over the lifetime of the in-force policies is amortised and the discount unwound on a systematic basis over the anticipated lives of the related contracts, which in the case of the acquisition of ABC Insurance Company Limited, the directors have determined to be 15 years.

ABI, 198

The carrying value of the asset is assessed annually using current assumptions in order to determine whether any impairment has arisen compared to the amortised acquired value based on assumptions made at the time of the acquisition.

ABI, 200

Any amortisation or impairment charge is recorded in the long-term business technical account in 'Other technical charges'.

As noted in our commentary on the balance sheet, the ABI SORP provides guidance on the accounting treatment of the present value of acquired in-force business. The recognised acquired asset comprises two components in which the shareholders have an interest:

- the surplus emerging from the in-force contracts; and
- the 'estate'.

ABI, 198

Both of these components are recognised in the balance sheet, but only the first is expected to be systematically amortised. The amortisation is to be determined on a systematic basis over the anticipated lives of the in-force contracts.

The amortisation requirement might be seen as being designed in principle to match with the post-acquisition emergence and distribution of surplus to shareholders from the acquired contracts, and so ensuring that reported post-acquisition profits are not distorted.

In the case of the 'estate', no such profits are expected to arise post-acquisition. Accordingly, no systematic amortisation is required, but there is nonetheless a requirement to consider whether the value of the shareholders' interest in the estate has been impaired, inter alia, by any distribution of the estate which has occurred in practice, for example in support of terminal bonuses in excess of those supported by asset shares.

In considering the carrying value of the acquired in-force contracts at balance sheet dates subsequent to acquisition, account also needs to be taken of the unwind, with the passage of time, of the discount implicit in the present value at the time of acquisition.

ABI, 198

The ABI SORP states that 'the asset should be amortised and the discount unwound . . . on a systematic basis'. The ABI SORP then goes on to set out various disclosure requirements in respect of the amortisation. It is unclear whether these disclosure requirements encompass the unwind of the discount as part of the amortisation or separate from it. In these illustrative accounts, we have treated the amortisation and unwind of the discount together.

PwC In the case of the Proforma-Life Group, in the period since acquisition of the in-force portfolio, the amortisation has exceeded the unwind of the discount. Circumstances might arise when the unwind of the discount exceeds the amortisation, resulting in an overall increase in the value of the acquired in-force business. The ABI SORP provides no guidance on how this increase in value should be recognised. In our view, recognition of such an increase in value in the technical account is inappropriate.

PwC We would therefore envisage that insurers may wish to systematically recognise any overall reduction in the carrying value of the asset (taking the amortisation and unwind of the discount together) as amortisation in the technical account, but may not consider it appropriate to recognise any overall increase in value.

Self-generated PVIF

ABI, 199
ABI, 151
Self-generated PVIF should not be recognised as an asset in the balance sheet. The only exception to this is the option to recognise an asset representing the value of non-profit business written out of a with-profits fund in accordance with FRS 27.

M. Present value of future profits on non-profit business written out of the with-profits fund

FRS 27, 4(d)

In determining the realistic value of liabilities for with-profits contracts, indirect account is taken of the value of future profits on non-profit business written out of the with-profits fund. Although not separately identifiable, the fund for future appropriations includes the excess of the value of those future profits that are taken into account in calculating the realistic liabilities. Since it is not possible to apportion the future profits on this non-profit business between the amount relating to policyholder liabilities and the amount relating to the FFA, the present value of future profits (PVFP) on this business is recognised as an asset.

The value of the PVFP is determined in accordance with the FSA's realistic capital regime. In particular, the methodology and assumptions involve adjustments to reflect risk and uncertainty, are based on current estimates of future experience and current market yields and allow for a market-consistent valuation of any guarantees or options within the contracts. The value is also adjusted to remove the value of the capital backing the non-profit business if this is included in the FSA calculation of PVFP.

N. Tangible assets

FRS 15, 100(a) &100(b)

Tangible assets are capitalised and depreciated by equal annual instalments over their estimated useful lives. The principal rates used for this purpose are as follows:

	%
Motor vehicles	25
Computer equipment	$33^{1/3}$
Fixtures, fittings and office equipment	10

FRS 15 'Tangible fixed assets' sets out the principles of accounting for the initial measurement, valuation and depreciation of tangible fixed assets. Investment properties continue to be accounted for in accordance with SSAP 19.

FRS 15, 31 Where finance costs are capitalised, the following information should be disclosed:

- accounting policy adopted;
- aggregate amount of finance costs included in the cost of tangible fixed assets;
- the amount of finance costs capitalised during the period;
- the amount of finance costs recognised in the profit and loss account during the period; and
- the capitalisation rate used to determine the amount of finance costs capitalised during the period.

FRS 11, 8 Impairment reviews should be carried out if events or changes indicate that the carrying amount of fixed assets or goodwill may not be recoverable.

FRS 11, 14 Any excess of carrying value over recoverable amount should be written down.

FRS 11, 1 It is anticipated that, for tangible fixed assets, impairments will be relatively infrequent.

The requirements for review also extend to fixed asset investments in group undertakings and participating interests in the parent company balance sheet, where that balance sheet is prepared in accordance with Schedule 4.

O. Surpluses from long-term business and the fund for future appropriations

Surpluses arising from the Group's with-profits business, as a result of the annual actuarial valuations of the related assets and liabilities, are subject to appropriation, by the directors of the relevant subsidiary undertakings, to with-profits policyholders by way of bonuses and to shareholders, which determines their profit reported in respect of this business.

Any unappropriated surplus arising in long-term funds which include with-profits business is carried forward in the fund for future appropriations. All surplus in other businesses is attributable to shareholders and included in profit.

ABI, 195 The fund for future appropriations represents all funds, the allocation of which to with-profits policyholders and shareholders has not been determined at the balance sheet date. Transfers between the fund for future appropriations and the long-term business technical account represent the changes in these unallocated amounts between balance sheet dates.

P. Long-term business provision

With-profits business

For with-profits contracts (contracts with discretionary participation features), the long-term business provision is calculated in accordance with the FSA's 'realistic' liability regime. In particular, provision is made for all future contractual and discretionary payments consistent with the Principles and Practice of Financial Management ('PPFM'). The realistic liabilities are based on the aggregate value of policy asset shares reflecting the premiums, investment return, expenses and charges applied to each policy. Allowance is also made for policy-related liabilities such as the time and intrinsic values of guarantees and options and future bonuses. These are calculated using a stochastic model simulating future investment returns, asset mix and bonuses and allowing for future management actions in line with the PPFM.

The liability is also reduced to the extent that the 'realistic' assessment includes an amount that may subsequently be attributed to shareholders; this amount is retained within the fund for future appropriations ('FFA').

The long-term business provision includes liabilities in respect of with-profits investment contracts where there is no significant insurance risk transfer but which allow the policyholder to participate in the surplus arising from the assets held in the investment with-profits fund.

Value of in-force business

Since the realistic liabilities include an allowance for future bonuses to with-profits policyholders that will be payable out of returns on non-profit business, an asset is recognised representing the value of non-profit business written within the with-profits fund.

Such an asset is not recognised for business written outside the with-profits fund.

Options and guarantees

Some with-profits policies contain options and guarantees that can increase the benefits payable to the policyholder. As noted above, a market consistent stochastic model is used to determine the potential liability for these options and guarantees. The most significant options and guarantees are:

- with-profits deferred annuity policies where the annuity is at a guaranteed minimum rate;
- with-profits policies with minimum surrender values;
- unitised with-profits policies containing a guaranteed increase in the unit price or a guarantee that the unit price will not fall; and
- the sum assured and declared reversionary bonuses on with-profits policies.

Non-profit business

FRS 27, 51

For conventional non-profit business, a gross premium valuation method is used, which brings into account the full premiums receivable under contracts written by the company, estimated renewal and maintenance costs and contractually guaranteed benefits.

In addition, where appropriate, adjustment is made to the long-term business provision so as to measure the liabilities on a basis consistent with the adoption of an amortised cost valuation basis for certain corresponding categories of assets.

Some products written outside the with-profits fund contain options and guarantees. The most significant are contracts containing the option to purchase an annuity at a guaranteed rate. These contracts are valued stochastically using a similar approach to that described above for with-profits business. The key factors impacting the valuation are the interest rate, which is modelled stochastically, and the option take-up rate.

The long-term business provision includes the non-unit liabilities in respect of unit-linked insurance contracts.

PwC

As unit-linked investment contracts are not within the accounting regime for insurance contracts, it should not be necessary to establish sterling reserves on a prudent regulatory basis for such contracts for accounting purposes.

Sch9A BS(21)

Schedule 9A requires that the long-term business provision shall comprise the actuarially estimated value of the company's liabilities excluding linked liabilities. In practice, many insurers use as a starting point the provisions determined for regulatory purposes, but there is no requirement to do so. Separate bases may be used for the insurance annual returns and the financial statements. When the starting point is the regulatory provision, however, as is noted in the ABI SORP and in actuarial guidance (GN7), the reporting actuary needs to modify these regulatory provisions to comply with the modified statutory solvency basis of accounting ('MSSB') .

Such modifications are likely to include:

- the exclusion of items which fall properly to be treated as reserves and not provisions, such as investment and business closure contingency reserves. Paragraph 183 of the ABI SORP provides further guidance; and
- modification to enable the liabilities to be assessed on a basis consistent with the bases adopted for valuing corresponding assets. In particular, the amortised cost valuation basis may not be used for regulatory valuation purposes, market values are used and the actuarial liabilities are determined using market-based interest yields. In principle, therefore, where for financial statements purposes the amortised cost valuation basis is used for assets, the valuation interest rates should be adjusted.

FRS 27 'Life assurance'

FRS 27, 4(a)

FRS 27 integrates financial statements accounting with the regulatory regime as presented in INSPRU. In particular, the insurance liability for with-profits contracts of large UK with-profits funds is required to be based on the FSA's definition of a 'realistic' valuation.

For such funds, the liability:

- includes a provision for all bonus payments (declared and future, reversionary and terminal) estimated, where necessary, in a manner consistent with the company's Principles and Practice of Financial Management ('PPFM'). Cash flows are projected using best estimate assumptions;
- includes an allowance for the fair value of any guarantees or options granted to the policyholders; and
- FRS 27, 10 — is adjusted to the extent that the 'realistic' assessment includes an amount that may subsequently be attributed to shareholders (e.g. through the shareholders' share of future bonuses). This amount will be retained within the FFA.

The effect of FRS 27's requirements on the valuation of liabilities is included in the profit and loss account. However, an offsetting transfer, equal to the net amount of these adjustments, is made to or from the FFA (and so also included in the profit or loss account) with the result that there is no change in the reported profit or loss as a result of the application of FRS 27's requirements.

FRS 27, 4(e) — Where a with-profits fund has an interest in a subsidiary or associated entity that is valued for FSA regulatory purposes at an amount in excess of the net amounts that would be included in the consolidated accounts, FRS 27 permits recognition of an amount representing this excess if the determination of the realistic value of liabilities to with-profits policyholders takes account of this value.

Prudential Requirements for Insurers (Amendment) instrument 2006 (2006/62)

The FSA introduced some significant relaxations to the 'Pillar 1' regulatory peak reserving requirements for life insurers with effect from 31 December 2006. The principal changes were:

- setting technical provisions for expenses not directly attributable to one particular contract at a homogenous risk group level and not, as previously, at an individual contract level for all long-term business;
- recognising the economic effect of making a prudent lapse rate assumption within technical provisions for all classes of long-term business. Previously lapses could be assumed only for the with-profits business of realistic basis life firms, except where lapses would increase the mathematical reserves; and
- changing the calculation of technical provisions for all classes of long-term business to allow contracts that do not include a surrender value guaranteed in the contract wording at the valuation date to have negative mathematical reserves. Previously such contracts were recognised at a zero value.

The FSA's rules set out the minimum basis for mathematical reserves and methods and assumptions that produce reserves equal to or greater than this minimum basis may be used. While the majority of companies (including Proforma-Life Limited) which plan to adopt any or all of the changes have already done so, it is possible that some will seek to apply them for the first time in 2008.

To the extent that any insurers do adopt these changes in the regulatory return for the first time at the 2008 year-end, they will need to consider the impact on their financial statements. The ICAEW Technical Release FSF 02/07 "Accounting Implications of Changes to the Financial Services Authority's Rules for Calculating Technical Provisions" deals with the accounting implications of these changes. In particular FSF 02/07 highlights that:

- FSF 02/07, 11 — under the Modified Statutory Solvency Basis of accounting set out in the ABI SORP there is a presumption that any changes to mathematical reserves will flow through to the long-term business provision unless such changes represent reserves which have already been adjusted;
- FSF 02/07, 12; ABI 182 — paragraph 182 of the ABI SORP allows a policy to have an overall negative value if allowed by FSA rules, in determining the long-term business provision;
- FSF 02/07, 17 — the change in methodology in determining the long-term business provision is considered to be a change in estimation technique and not a change in accounting policy;
- FSF 02/07, 19 — a consequence of changing the assumption set used to calculate the LTBP is that it might be necessary to reassess the recoverability of deferred acquisition costs; and

FSF 02/07, 21-22

- careful consideration will need to be given to the adequacy of disclosure of the basis of determination of the LTBP, the decision on whether to adjust the LTBP for financial reporting purposes will represent a material estimation technique.

FSF 02/07, 6
PwC

These changes in regulation should not lead to any changes in the measurement of “investment contracts” under FRS 26 or to with-profits liabilities that are measured on a realistic basis.

Other requirements

ABI, 180

For contracts which are not required by FRS 27 to be included at their realistic value, the gross premium valuation method should be used for all classes of business except those for which the net premium method is used in the regulatory returns.

ABI, 184

The ABI SORP provides further guidance as to the disclosures that should be provided in the summary of the principal assumptions underlying the long-term business provision (LTBP).

This includes, for each principal category of business, the more significant assumptions relating to premiums, persistency, mortality and morbidity, interest rates, discount rates used and any other significant factors. A brief explanation (which may be qualitative) should be provided of any changes in significant assumptions or bases of preparation and the sensitivity of the amount reported with respect to changes in the principal assumptions or bases of preparation.

ABI, 186

For with-profits contracts not required by FRS 27 to be included at their realistic value (e.g. small funds or overseas business), the ABI SORP requires further disclosure of the calculation of the long-term business provision, including future bonuses.

PwC

The long-term business provision is not considered the appropriate heading for the inclusion of financial liabilities in relation to investment contracts under FRS 26, principally due to the valuation basis prescribed for this line item under Schedule 9A.

Q. Technical provisions for linked liabilities

Liabilities under unit-linked contracts are recognised as and when the units are created and are dependent on the value of the underlying financial assets, derivatives and/or investment property.

Unit-linked contracts which transfer significant insurance risk, including guaranteed benefits, are classified as insurance contracts and are carried in the balance sheet at an amount determined by the valuation of the related units on the valuation date.

Unit-linked contracts which principally involve the transfer of financial risk are classified as investment contracts and are carried in the balance sheet at amortised cost. The amortised cost of these financial liabilities is equivalent to the amount payable on demand without penalty.

R. Financial liabilities

FRS 26, 43, 47

Borrowings are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortised cost, any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the profit and loss account over the period of the borrowings using the effective interest method.

Preference shares, which are mandatorily redeemable on a specific date, are classified as liabilities. The dividends on these preference shares are recognised in the profit and loss account as interest expense.

Other financial liabilities, carried at amortised cost, relate to unit-linked investment contracts under ‘Technical provisions for linked liabilities’ (see Accounting policy Q ‘Technical provisions for linked liabilities’ above) and creditors.

FRS 26 Measurement of financial liabilities

See Accounting policy I 'Investments' above for discussion of the provisions of FRS 26 relating to recognition and derecognition and to the initial measurement of financial instruments (including financial liabilities).

Subsequent measurement

After initial recognition, an entity shall measure all financial liabilities at amortised cost using the effective interest method, except for:

FRS 26, 47

(a) financial liabilities at fair value through profit or loss. Such liabilities, including derivatives that are liabilities, shall be measured at fair value except for a derivative liability that is linked to and must be settled by delivery of an unquoted equity instrument whose fair value cannot be reliably measured, which shall be measured at cost; and

(b) financial liabilities that arise when a transfer of a financial asset does not qualify for derecognition.

Financial liabilities that are designated as hedged items are subject to measurement under the hedge accounting requirements (see notes to Accounting policy K 'Derivative financial instruments').

Sch9A, 29A (3)

The rules in the Companies Act 1985 permitting financial liabilities to be included at fair value only extend to derivatives and financial liabilities held as part of a trading portfolio.

Undated subordinated loan notes

PwC

In order to raise capital loan notes for regulatory return purposes, many insurance groups have issued subordinated loan notes. In some instances, the coupon payable on such debt can be deferred which may result in them being treated as equity rather than debt under the presentation requirement of FRS 25. It is therefore necessary to consider carefully the detailed terms of any undated subordinated loan notes to ensure that the classification of such instruments under FRS 25 is appropriate.

Proforma-Life Limited has not issued any undated subordinated loan notes.

S. Taxation

FRS 19, 37
FRS 19, 34
FRS 19, 52

Provision is made for deferred tax liabilities, using the liability method, on all material timing differences, including revaluation gains and losses on investments recognised in the profit and loss account. Deferred tax is calculated at the rates at which it is expected that the tax will arise and discounted to take into account the likely timing of payments and the pattern of the expected realisation of investments. The discount rates used are the post-tax yields to maturity that could be obtained at the balance sheet date on government bonds with maturity dates and in currencies similar to those of the deferred tax assets or liabilities.

Deferred tax is recognised in the profit and loss account for the period, except to the extent that it is attributable to a gain or loss that is recognised directly in the statement of total recognised gains and losses.

ABI 188, 189

The deferred tax recognised excludes the effect of the timing of tax relief where assumed expenses exceed attributable income recognised within the long-term business provision.

FRS 19, 35

Where a gain or loss has been recognised directly in the statement of total recognised gains and losses, deferred tax attributable to that gain or loss should also be recognised directly in that statement.

FRS 19, 42, 44

Companies are permitted, but not required, to discount deferred tax assets and liabilities to reflect the time value of money. If discounting is adopted, all deferred tax balances that have been measured by reference to undiscounted cash flows and for which the impact of discounting is material should be discounted.

ABI, 298

Investment return allocated from the long-term business technical account to the non-technical account in order to reflect the longer-term rate of return is stated gross of attributable tax.

ABI, 210

The transfer of the balance on the long-term business technical account to the non-technical account is grossed up by attributable tax, using the effective rate of tax applicable for the period.

T. Pension costs

FRS 17, 76(a)

The Group operates a defined benefit pension scheme. The pension asset recognised in the balance sheet is the value of the scheme's assets less the present value of the scheme's liabilities.

The pension cost for the scheme is analysed between current service cost, past service cost and net return on pension scheme. Current service cost is the actuarially calculated present value of the benefits earned by the active employees in each period. Past service costs, relating to employee service in prior periods arising in the current period as a result of the introduction of, or improvement to, retirement benefits, are recognised in the profit and loss account on a straight-line basis over the period in which the increase in benefits vest.

Net expected return on the pension asset comprises the expected return on the pension scheme assets less interest on scheme liabilities.

The actuarial gains and losses which arise from a valuation and from updating the latest actuarial valuation to reflect conditions at the balance sheet date are taken to the statement of total recognised gains and losses for the period to the extent they are attributable to shareholders. The attributable deferred taxation is shown separately in the statement of total recognised gains and losses. Actuarial gains or losses which are not attributable to shareholders are included as a separate line in the technical account for long-term insurance business immediately above the line for transfer to or from the fund for future appropriations and are reflected in that transfer.

U. Foreign currencies

FRS 23
ABI, 219
Sch9A, 57

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates. Pounds sterling is the functional currency of all Group entities, with the exception of Proforma-Life Ireland Company Ltd (Ireland) whose functional currency is the Euro. The consolidated financial statements are presented in millions of pounds sterling, which is the Group's presentation currency. The assets and liabilities of Proforma-Life Ireland Company Ltd (Ireland) are translated into pounds sterling at the closing rate and its profit and loss account is translated at average rates with the resulting exchange differences taken to the statement of total recognised gains and losses.

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the profit and loss account for the period

Translation differences on non-monetary items, such as equities held at fair value through profit or loss, are reported as part of the fair value gain or loss.

FRS 23 'The effects of changes in foreign exchange rates'

FRS 23 is part of the package of standards that, broadly speaking, have to be implemented at the same time as, and the effective date is determined by reference to, FRS 26's application.

FRS 23, 8

FRS 23 derives from IAS 21 and it sets out the requirements for initial recognition, subsequent measurement and disclosure relating to foreign currency translation. It requires each entity within the Group to determine its functional currency and measure its results in that currency. The functional currency is the currency of the primary economic environment in which the entity operates. Proforma-Life Limited has an Irish subsidiary which operates in that country, with cash being generated and expended in Euros and, therefore, the functional currency of the Irish subsidiary is Euros.

FRS 23, 23

An entity may present its financial statements in any currency (the 'presentation' currency), but is required to disclose the reasons for doing so. Foreign currency transactions should be translated at the exchange rate at the date of the transaction (or an average rate, if appropriate). Foreign currency monetary assets and liabilities are retranslated at the closing (period-end) rate and exchange differences are taken to the profit and loss account. Non-monetary items denominated in a foreign currency are measured at historical rates at either the transaction date or, for items measured at fair value, the exchange rate at the date when the value was determined. Exchange differences on non-monetary items should be recognised in either equity or in the profit and loss account depending on where the underlying gain or loss on the non-monetary item is recognised.

A foreign entity's assets and liabilities (both monetary and non-monetary) are translated into a different presentation currency at the closing rate and its profit and loss account is translated at actual (average) rate with resulting exchange differences classified as a separate component of equity. On disposal of a foreign entity, the cumulative translation difference relating to the entity is included in the gain or loss on sale in the profit and loss account. FRS 23 contains specific rules requiring goodwill and fair value adjustments arising on acquiring a foreign operation to be translated at the closing rate.

V. Operating leases

SSAP 21, 57

Rentals payable under operating leases are charged to the profit and loss account as incurred over the lease term.

W. Dividends

Tech 57/05

Interim dividends are recognised when paid and final dividends are booked as a liability when they are approved by the members passing a written resolution.

Notes to the financial statements
for the year ended 31 December 2008

1 Management of financial risk

1.1 Financial risk management objectives

Sch7, 5A(1)(a)
FRS 29, 31
FRS 29, AppA

The Group is exposed to a range of financial risks through its financial assets, financial liabilities (investment contracts and borrowings), reinsurance assets and policyholder liabilities. In particular, the key financial risk is that the proceeds from financial assets are not sufficient to fund the obligations arising from insurance policies and investment contracts as they fall due. The most important components of this financial risk are market risk (including interest rate risk, equity price risk and currency risk), credit risk and liquidity risk.

These risks arise from open positions in interest rate, currency and equity products, all of which are exposed to general and specific market movements. The risks that the Group primarily faces due to the nature of its investments and liabilities are interest rate risk and equity price risk.

The Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Group's financial performance. It manages these positions within an asset liability management (ALM) framework that has been developed to achieve investment returns in excess of obligations under insurance contracts. The Group produces regular reports at portfolio, legal entity and asset and liability class level that are circulated to the Group's key management personnel. The principal technique of the Group's ALM is to match assets to the liabilities arising from insurance contracts by reference to the type of benefits payable to contract holders. Separate portfolios of assets are maintained for with-profits business, non-linked non-profit business, and unit-linked business. For the purposes of the ALM framework, the Group does not manage the fund for future appropriations as a liability. The Group's ALM is also integrated with the management of the financial risks associated with the Group's other financial assets and liabilities not directly associated with insurance and investment liabilities. The Group does not use hedge accounting.

The Group has not changed the processes used to manage its risks from previous periods. The notes below explain how financial risks are managed using the categories utilised in the Group's ALM framework.

The following tables reconcile the balance sheet to each distinct category of liabilities:

2008

	With-profits business	Non-linked non-profit insurance contracts	Unit-linked contracts	Corporate	Total
	£m	£m	£m	£m	£m
Shares and other variable yield securities and units in unit trusts, at fair value through profit or loss:					
- listed securities	**642.3**	**253.3**	**892.5**	**3.2**	**1,791.3**
- unlisted securities	**221.0**	**139.1**	**355.1**	**0.4**	**715.6**
Debt securities and other fixed income securities – at fair value through profit or loss					
- listed securities	**123.9**	**82.3**	**413.2**	**0.5**	**619.9**
- unlisted securities	**1.1**	**1.2**	**-**	**1.2**	**3.5**
Derivative financial instruments, at fair value through profit or loss	**-**	**-**	**2.1**	**-**	**2.1**
Debt securities and other fixed income securities - held-to-maturity					
- listed securities	**52.2**	**47.2**	**-**	**8.2**	**107.6**
- unlisted securities	**1.3**	**2.1**	**-**	**1.1**	**4.5**
Loans and receivables	**59.0**	**17.3**	**-**	**12.1**	**88.4**
Deposits with ceding undertakings	**4.3**	**-**	**-**	**-**	**4.3**
Reinsurance assets	**76.7**	**30.2**	**-**	**-**	**106.9**
Other assets	**245.0**	**154.5**	**-**	**187.1**	**586.6**
Total assets	**1,426.8**	**727.2**	**1,662.9**	**213.8**	**4,030.7**
Long-term business provision	**1,141.2**	**485.7**	**-**	**-**	**1,626.9**
Claims outstanding	**12.9**	**3.2**	**-**	**-**	**16.1**
Technical provisions for linked liabilities	**-**	**-**	**1,653.6**	**-**	**1,653.6**
Provisions for other risks and charges	**28.7**	**17.1**	**-**	**16.1**	**61.9**
Deposits received from reinsurers	**12.2**	**3.0**	**-**	**-**	**15.2**
Borrowings	**-**	**-**	**-**	**112.6**	**112.6**
Other liabilities	**21.9**	**17.4**	**9.3**	**44.2**	**92.8**
Total liabilities	**1,216.9**	**526.4**	**1,662.9**	**172.9**	**3,579.1**

2007

	With-profits business	Non-linked non-profit insurance contracts	Unit-linked contracts	Corporate	Total
	£m	**£m**	**£m**	**£m**	**£m**
Shares and other variable yield securities and units in unit trusts, at fair value through profit or loss:					
- listed securities	505.4	207.3	975.7	2.8	1,691.2
- unlisted securities	167.9	104.5	196.7	0.3	469.4
Debt securities and other fixed income securities – at fair value through profit or loss					
- listed securities	139.0	70.9	241.7	0.6	452.2
- unlisted securities	1.6	2.1	-	1.3	5.0
Derivative financial instruments, at fair value through profit or loss	-	-	1.8	-	1.8
Debt securities and other fixed income securities - held-to-maturity					
- listed securities	48.8	32.4	-	8.7	89.9
- unlisted securities	2.7	2.0	-	1.4	6.1
Loans and receivables	65.0	19.4	-	14.8	99.2
Deposits with ceding undertakings	2.9	-	-	-	2.9
Reinsurance assets	70.1	26.1	-	-	96.2
Other assets	226.6	143.6	-	103.3	473.5
Total assets	1,230.0	608.3	1,415.9	133.2	3,387.4
Long-term business provision	976.2	398.5	-	-	1,374.7
Claims outstanding	7.5	2.6	-	-	10.1
Technical provisions for linked liabilities	-	-	1,411.7	-	1,411.7
Provisions for other risks and charges	21.3	13.0	-	13.0	47.3
Deposits received from reinsurers	12.0	4.0	-	-	16.0
Borrowings	-	-	-	60.1	60.1
Other liabilities	27.6	15.3	4.2	30.5	77.6
Total liabilities	1,044.6	433.4	1,415.9	103.6	2,997.5

FRS 29 ‘Financial instruments: Disclosures’

PwC FRS 29 focuses on improving the transparency of entities’ financial risk profiles by restructuring and extending the previous disclosure requirements in relation to financial instruments in three key areas: qualitative risk disclosures ‘through the eyes of management’; comprehensive quantitative disclosures; and the introduction of sensitivity analysis to market risks.

FRS 29, 31 FRS 29 requires information to be disclosed that enables users of its financial statements to evaluate the nature and extent of risks arising from financial instruments to which the entity is exposed at the reporting date. These typically include credit risk, liquidity risk and market risk.

FRS 25, 11 It should be remembered that the definition of a financial instrument is wide and includes simple instruments such as borrowings, other creditors and debtors, and cash, as well as more complex instruments. The disclosure requirements of FRS 29 apply equally to all financial instruments.

Qualitative disclosures

FRS 29, 33 For each type of risk an entity shall provide the following qualitative disclosures:

(a) the exposures to risk and how they arise;

(b) its objectives, policies and processes for managing risk and the methods used to measure the risk; and

(c) any changes in the approach to risk management from the previous period.

Quantitative disclosures

FRS 29, 34 For each type of risk arising from financial instruments, an entity shall provide summary quantitative data about its exposure to that risk at the reporting date, based on information provided internally to key management (those having authority and responsibility for planning, directing and controlling the activities of the entity directly or indirectly). If the quantitative information provided at the reporting date is not representative of the entity’s exposure to risk during the period, further information should be provided.

PwC Proforma-Life Limited manages its exposure to risk within an ALM framework and, accordingly, the quantitative data disclosed under FRS 29 para 34 reflects this basis of financial risk management. These disclosures are provided for illustrative purposes only and will not necessarily be applicable for all unlisted life insurance groups/companies. Entities will need to reflect their own individual circumstances and the specific framework in place for managing financial risk. Furthermore, it is likely that emerging best practice will develop over time.

Sensitivity analysis

FRS 29, 40 A sensitivity analysis is required for each component of market risk (currency, interest rate and other price risk) to which the entity is exposed at the reporting date, showing how profit or loss and equity would have been affected by changes in the relevant risk variable that were reasonably possible at that date. Proforma-Life Limited discloses three types of market risk - interest, equity price and currency risks. The methods and assumptions used in preparing the analysis and any changes from the previous period (with reasons for the changes) should be given.

FRS 29,41 If the entity prepares a sensitivity analysis which reflects interdependencies between risk variables (e.g. interest rates and exchange rates) and uses it to manage financial risks, this may be used provided an explanation of the objectives, limitations and methods, parameters and assumptions are given.

FRS 29, B19 In preparing the required quantitative sensitivity analysis, entities should select hypothetical movements in the underlying variables that reflect a ‘reasonably possible change in the relevant risk variable’. This needs to be based on the economic environment in which the insurer operates and the time frame over which it is making the assessment (usually the next annual reporting period). Recent market conditions may lead to a

PwC reassessment of what changes in variables are viewed as reasonably possible compared with the disclosures given in prior years.

PwC

Insurance risk

For IFRS reporters, insurance contract disclosures have been brought into line with the disclosure requirements for other financial instruments through an amendment to IFRS 4 'Insurance Contracts'. However there is no equivalent amendment to UK GAAP. For UK Life insurers reporting under UK GAAP, FRS 27 'Life insurance' sets out certain disclosure requirements in relation to policies and objectives for managing risks affecting the capital position of the entity and disclosures around the sensitivity of liabilities and capital to market conditions, assumptions and other variables. Some entities may choose to provide additional information on a voluntary basis. Proforma-Life Limited has not provided any additional voluntary disclosures.

Sch7, 5A(1)(b)

(a) Market risk

(i) Interest rate risk

FRS 29, 33(a)(b)

Interest rate risk arises primarily from investments in fixed interest securities. In addition to the extent that claims costs are related to interest rates, liabilities to policyholders are exposed to interest rate risk. Insurance and non-profit investment contracts have benefit payments that are fixed and guaranteed at the inception of the contract. The financial component of these benefits is usually a guaranteed fixed interest rate (for the insurance contracts, this rate may apply to maturity and/or death benefits) and hence the Group's primary financial risk on these contracts is the risk that interest income and capital redemptions from the financial assets backing the liabilities is insufficient to fund the guaranteed benefits payable. The Group monitors interest rate risk by calculating the mean duration of the investment portfolio and of the liabilities to policyholders under insurance and investment contracts. The mean duration is an indicator of the sensitivity of the assets and liabilities to changes in current interest rates. The mean duration of the liabilities is determined by means of projecting expected cash flows from the contracts using best estimates of mortality and voluntary terminations. This is calculated in a consistent manner with the prior year. Any gap between the mean duration of the assets and the estimated mean duration of the liabilities is minimised by means of buying and selling fixed interest securities of different durations.

Borrowings issued at variable rates expose the Group to cash flow interest rate risk. Borrowings issued at fixed rates expose the Group to fair value risk. Group policy is to increase the proportion of borrowings at fixed rates.

FRS 29, 40

The sensitivity analysis for interest rate risk illustrates how changes in the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates at the reporting date. For the guaranteed element of liabilities under with-profits contracts, changes in interest rate will not cause a change to the amount of the liability because their carrying amounts are not affected by the level of market interest rates. However the with-profits element of the liabilities is directly affected by changes in the level of interest rates to the extent that they affect the carrying amount of the assets held in the with-profits funds. Management monitors the sensitivity of reported interest rate movements on a monthly basis by assessing the expected changes in the different portfolios due to parallel movements of 100 basis points in all yield curves. An increase of 100 basis points in interest yields would result in additional profit for the period of £10.3m (2007: £7.5m). A decrease in 100 basis points in interest yields would result in an additional loss for the period of £11.1m (2007: £4.8m).

Sch7, 5A(1)(b)
FRS 29, 33

(ii) Equity price risk

The Group is exposed to equity securities price risk as a result of its holdings in equity investments, classified as financial assets at fair value through profit or loss. Exposures to individual companies and to equity shares in aggregate are monitored in order to ensure compliance with the relevant regulatory limits for solvency purposes. Investments held are listed and traded on the UK and other recognised stock exchanges (primarily in Europe and North America).

The Group has a defined investment policy which sets limits on the Group's exposure to equities both in aggregate terms and by geography, industry and counterparty. This policy of diversification is used to manage the Group's price risk arising from its investments in equity securities.

Investment Management meetings are held monthly. At these, senior investment managers representing all Group companies meet to discuss investment return and concentration across the Group.

FRS 29, 34(a), 40

The sensitivity analysis for equity risk illustrates how changes in the fair value of equity securities will fluctuate because of changes to market prices, whether those changes are caused by factors specific to the individual equity issuer, or factors affecting all similar equity securities traded in the market. Management monitors equity price movements on a monthly basis by assessing the expected changes in the different portfolios arising from a 5% movement in the various stock exchange indices. Listed equity securities represent 71% (2007: 78%) of total equity investments. If equity market indices had increased/decreased by 5%, with all other variables held constant, and all the Group's equity investments moving according to the historical correlation with the index, the profit for the year would increase/decrease by £39.6m (2007: £34.6m).

(iii) ***Currency risk***

Sch7, 5A(1)(b) FRS 29, 33(a)(b)

The management has set up a policy to require Group companies to manage their foreign exchange risk against their functional currency. Foreign exchange risk arises when future commercial transactions or recognised assets and liabilities are denominated in a currency that is not the entity's functional currency.

The Group is primarily exposed to currency risk in respect of liabilities under policies of insurance denominated in currencies other than Sterling. The most significant currency to which the Group is exposed is the Euro. The Group seeks to mitigate the risk by matching the estimated foreign currency denominated liabilities with assets denominated in the same currency. The Group has an Irish subsidiary, whose net assets are exposed to foreign currency translation risk. Currency exposures are managed primarily through borrowings, although the Group has no designated hedging contracts.

FRS 29, 40

At 31 December 2008, if the pound had weakened/strengthened by 4% against the Euro with all other variables held constant, profit for the year would have been £1.7m (2007: £0.6m) lower/higher, mainly as a result of foreign exchange gains/losses on the translation of Euro denominated financial assets, carried at fair value through profit or loss and foreign exchange losses/gains on translation of Euro denominated borrowings.

(b) Credit risk

Sch7, 5A(1)(b) FRS 29, 33(a)(b)

Credit risk is the risk that a counterparty will be unable to pay amounts in full when due. Key areas where the Group is exposed to credit risk are:

- amounts due from insurance intermediaries;
- amounts due from corporate bond issuers;
- amounts due from insurance contract holders;
- reinsurers' share of insurance and investment contract liabilities; and
- amounts due from reinsurers in respect of claims already paid,

The Group manages the levels of credit risk it accepts by placing limits on its exposure to a single counterparty, or groups of counterparties and to geographical and industry segments. Such risks are subject to regular review. Limits on the level of credit risk by category and territory are approved quarterly by the Board of Directors.

Reinsurance is used to manage insurance risk. This does not, however, discharge the Group's liability as primary insurer. If a reinsurer fails to pay a claim, the Group remains liable for the payment to the policyholder. The creditworthiness of reinsurers is considered on an annual basis by reviewing their financial strength prior to finalisation of any contract. In addition, management assesses the creditworthiness of all reinsurers and intermediaries by reviewing credit grades provided by rating agencies and other publicly available financial information. The recent payment history of reinsurers is also used to update the reinsurance purchasing strategy.

Exposures to individual policyholders and groups of policyholders are collected within the ongoing monitoring of the controls associated with regulatory solvency. Where there exists significant exposure to individual policyholders, or homogenous groups of policyholders, a financial analysis equivalent to that conducted for reinsurers is carried out by the management. An analysis of policyholders and reinsurers by Standard & Poors (S&P) rating (or equivalent when not available from S&P) is produced periodically.

The assets bearing credit risk are summarised below, together with an analysis by credit rating:

FRS 29, 36

	Total	
	2008	**2007**
	£m	**£m**
Derivative financial instruments	**2.1**	1.8
Debt securities	**735.5**	553.2
Loans and receivables	**88.4**	99.2
Assets arising from reinsurance contracts held	**106.9**	96.2
Cash at bank and in hand	**62.1**	92.3
Total assets bearing credit risk	**995.0**	842.7
AAA	**706.8**	596.8
AA	**144.6**	133.9
A	**81.1**	66.5
BBB	**48.1**	42.4
Below BBB or not rated	**14.4**	3.1
Total assets bearing credit risk	**995.0**	842.7

The concentration of credit risk is substantially unchanged compared to prior year. No credit limits were exceeded during the period. No financial assets are past due or impaired at the reporting date and management expects no significant losses from non-performance by these counterparties.

PwC

The assets reported above include £415.3m (2007: £243.5m) related to the assets backing unit linked contracts. The holders of these contracts bear the credit risk arising from these assets. The assets above also include assets held in the with-profits funds where the Group is able to transfer part of the credit risk arising from these assets to holders of with-profits investment and insurance contracts to the extent that the future level of discretionary bonuses can be reduced to absorb any associated credit losses (as well as losses arising from all other financial risks). Details of the asset composition of with-profits funds are shown in the ALM tables on pages 68 and 69.

The Group maintains strict control limits on open derivative positions, by both amount and term. The amount subject to credit risk at any one time is limited to the current fair value of derivative financial assets.

FRS 29, 36	An entity shall disclose, by class of financial instrument, the amount that best represents its maximum exposure to credit risk at the reporting date together with a description of collateral held as security and other credit enhancements (e.g. guarantees). Information about the credit quality of financial assets that are neither past due nor impaired and the amount of renegotiated financial assets which would otherwise be past due or impaired should be disclosed.
FRS 29, 37	Where financial assets are past due, details of the age analysis are required. Where financial assets are impaired an analysis including factors considered in the determining that they are impaired should be given. A description of any collateral held by the entity as security or credit enhancements relating to such financial assets, together with the related fair values, is required.
FRS 29, 38	Information is required of any collateral and other credit enhancements obtained during the period.
PwC	The definition of equity in FRS 25 requires that the issuer has no obligation to pay cash or transfer other assets. It follows that equity investments are subject to price risk, not credit risk. Hence, most of the FRS 29 credit risk disclosures are not relevant to investments in equity instruments. The exception is the requirement to disclose an analysis of financial assets that are impaired. This disclosure is relevant and should be given for any impaired equity investments classified as available for sale.

Sch7, 5A(1)(b)

FRS 29, 33(a)(b), 39

(c) Liquidity risk

Liquidity risk is the risk that cash may not be available at a reasonable cost to pay obligations when due. The Board sets limits on the minimum proportion of maturing funds available to meet such calls and on the minimum level of borrowing facilities that should be in place to cover anticipated liabilities and unexpected levels of demand. The table below provides a contractual maturity analysis of the Group's financial liabilities:

	< 6mths or on demand	Between 6mths and 1 year	Between 1year and 2years	Between 2years and 5years	> 5 years	Total	Carrying value
	£m	£m	£m	£m	£m	£m	£m
At 31 December 2008							
Debenture and other loans	**2.2**	**2.7**	**5.3**	**29.6**	**23.7**	**63.5**	**58.5**
Bank loans and overdrafts	**14.3**	**40.8**		**-**	**-**	**55.1**	**54.1**
Financial liabilities under non-profit investment contracts	**967.1**	**-**	**-**	**-**	**-**	**967.1**	**967.1**
Creditors	**72.3**	**6.4**	**-**	**-**	**-**	**78.7**	**78.7**
Financial liabilities, at amortised cost	**1,055.9**	**49.9**	**5.3**	**29.6**	**23.7**	**1,164.4**	**1,158.4**
Financial liabilities under with-profits investment contracts included in LTBP	**368.2**	**-**	**-**	**-**	**-**	**368.2**	**382.5**
	1,424.1	**49.9**	**5.3**	**29.6**	**23.7**	**1,532.6**	**1,540.9**
At 31 December 2007							
Debenture and other loans	1.5	1.8	3.3	33.9	-	40.5	38.5
Bank loans and overdrafts	4.1	18.5	-	-	-	22.6	21.6
Financial liabilities under non-profit investment contracts	809.8	-	-	-	-	809.8	809.8
Creditors	57.4	8.1	-	-	-	65.5	65.5
Financial liabilities, at amortised cost	872.8	28.4	3.3	33.9	-	938.4	935.4
Financial liabilities under with-profits investment contracts included in LTBP	318.7	-	-	-	-	318.7	331.7
	1,191.5	28.4	3.3	33.9	-	1,257.1	1,267.1

FRS 29, 39

A maturity analysis for financial liabilities showing the remaining contractual maturities should be given, together with a description of how the liquidity risk is managed. There is no requirement to provide a maturity analysis of financial assets although some companies may choose voluntarily to disclose such information.

FRS 29, B14

The analysis should include the undiscounted cash flows at the earliest contractual payment date. As a result, the cash flows will differ from the amount included in the balance sheet as the balance sheet amount is based on discounted cash flows. No reconciliation is required.

FRS 29, B12

When there is a choice of when an amount is paid, the liability is included on the basis of the earliest date on which the entity can be required to pay.

PwC

Insurance entities will need to consider the time band into which the earliest contractual repayment date for financial liabilities under investment contracts (including with-profits investment contracts) would fall. This could be the earliest time band set out in the table to reflect a surrender option that makes each contract payable on demand. As a result some companies may also choose to voluntarily disclose the expected settlement date.

There is no requirement to provide a maturity analysis of liabilities under insurance contracts although some companies may choose voluntarily to disclose this information.

FRS 29, B13

When an entity is committed to making payments by instalments, each instalment is allocated to the earliest period in which the entity can be required to pay.

(d) Unit-linked contracts

PwC

For unit-linked contracts the Group matches all the liabilities with assets in the portfolio on which the unit prices are based. There is therefore no interest, price, currency or credit risk for the Group on these contracts.

Amounts under unit-linked contracts are generally repayable on demand and the Group is responsible for ensuring there is sufficient liquidity within the asset portfolio to enable liabilities to unit linked policyholders to be met as they fall due. However, the terms of funds investing in less liquid assets permit the deferral of redemptions for predefined periods in circumstances where there are not sufficient liquid assets within the fund to meet the level of requested redemptions.

PwC

Whilst the holders of unit-linked contracts bear the financial risks arising from assets backing their contracts, such assets are not excluded from the scope of FRS 29's disclosure requirements in respect of financial assets. Similarly liabilities under unit linked investment contracts are within the scope of FRS 29 disclosure requirements in respect of financial liabilities. Such disclosures provide the relevant policyholders with information concerning the risks associated with their investments. Where the terms of unit linked policies permit for the deferral of payment to policyholders in certain circumstances (as may be the case in respect of certain property backed funds) consideration should be given as to how this should be reflected in the liquidity disclosures given under FRS 29.

(e) Capital management

FRS 29, 42A, E1, E2

Proforma-Life Limited maintains an efficient capital structure from a combination of equity shareholders' funds and borrowings, consistent with the Group's risk profile and the regulatory and market requirements of its business.

The Group and the regulated entities within it are subject to a number of regulatory capital tests and also employ a number of realistic tests to allocate capital and manage risk. The Group and regulated entities within it have met all of these requirements throughout the financial year.

In reporting our financial strength, capital and solvency is measured using the regulations prescribed by the Financial Services Authority (FSA). These regulatory capital tests are based upon required levels of solvency capital and a series of prudent assumptions in respect of the type of business written by the company.

FRS 27, 45(d)

Capital management policies and objectives

The Group's objectives in managing its capital are:

- to match the profile of its assets and liabilities, taking account of the risks inherent in the business;
- to maintain financial strength to support new business growth;
- to satisfy the requirements of its policyholders, regulators and rating agencies;
- to retain financial flexibility by maintaining strong liquidity and access to a range of capital markets;
- to allocate capital efficiently to support growth; and
- to manage exposures to movement in exchange rates.

An important aspect of the Group's overall capital management process is the setting of target risk-adjusted rates of return for individual business units, which are aligned to performance objectives and ensure that the Group is focused on the creation of value for shareholders.

The Group has a number of sources of capital available to it and seeks to optimise its debt to equity structure in order to ensure that it can consistently maximise returns to shareholders. The Group considers not only the traditional sources of capital funding but the alternative sources of capital including reinsurance and securitisation, as appropriate, when assessing its deployment and usage of capital.

Restrictions on available capital resources

Proforma Life is required to hold sufficient capital to meet the FSA's capital requirements. Under the FSA's realistic reporting regime, the capital requirement for with-profits business is effectively determined such that capital resources must be sufficient to cover the greater of the statutory and realistic liability and capital requirements. For non-profit business, the capital requirement is calculated on the statutory basis, which is based on EU Directives. For all regulated insurance business, account is also taken of the Individual Capital Assessment which considers certain business risks not reflected in the statutory and realistic bases.

The available capital is subject to certain restrictions as to its availability to meet capital requirements. In particular, no transfers from long-term funds can take place without an up to date actuarial valuation.

The available surplus held in the with-profits fund can only be applied to meet the requirements of the fund itself or be distributed to policyholders and shareholders. Shareholders are entitled to an amount not exceeding one-ninth of the amount distributed to policyholders in the form of bonuses on conventional policies.

For non-profit business, the majority of surplus can be distributed to shareholders subject to meeting the requirements of the business.

The capital held within the shareholders' funds is generally available to meet any requirements. It remains the intention of management to ensure that there is adequate capital to exceed the Group's regulatory requirements.

The Group's total available capital resources are £416.1m (2007: £357.6m) of which £381.6m (2007: £332.4m) is held by the insurance funds. The capital held by the insurance business is constrained by regulatory requirements. This means it may not be possible for the capital to be used to provide funding for other businesses.

Available capital resources - 2008

	With-profits 2008	UK other 2008	Ireland 2008	Life Business Shareholder Funds 2008	Total life business 2008	Other activities 2008	Group total 2008
	£m	£m	£m	£m	£m	£m	£m
Shareholders' funds outside fund	–	–	–	**25.3**	**25.3**	**34.7**	**60.0**
Shareholders' funds Held in fund	–	**260.3**	**11.2**	–	**271.5**	–	**271.5**
Total shareholders' funds	–	**260.3**	**11.2**	**25.3**	**296.8**	**34.7**	**331.5**
Adjustments onto regulatory basis:							
FFA	**113.9**	–	–	–	**113.9**	–	**113.9**
Adjustment to assets	**23.0**	**(53.2)**	**(0.8)**	–	**(31.0)**	**(0.2)**	**(31.2)**
Other adjustments	**1.9**	–	–	–	**1.9**	–	**1.9**
Other qualifying capital:							
Internal loans	**25.0**	–	–	**(25.0)**	–	–	–
Total available capital resources	**163.8**	**207.1**	**10.4**	**0.3**	**381.6**	**34.5**	**416.1**

FRS 27, 53

Liability analysis – 2008

	With-profits	**UK other**	**Irish**	**Total life business**
	£m	**£m**	**£m**	**£m**
With-profits liabilities on realistic basis:				
Options and guarantees	**102.7**	**–**	**–**	**102.7**
Other policyholder obligations	**1,038.5**	**–**	**–**	**1038.5**
Total with-profits liabilities	**1,141.2**	**–**	**–**	**1,141.2**
Unit-linked insurance contracts	**–**	**612.4**	**74.1**	**686.5**
Unit-linked investment contracts	**–**	**793.2**	**173.9**	**967.1**
Non-profit life assurance	**–**	**412.9**	**72.8**	**485.7**
Technical provisions in balance sheet	**1,141.2**	**1,818.5**	**320.8**	**3,280.5**

At 31 December 2008, the realistic value of the with-profits liabilities was £1,141.2m (2007: £976.2m) on an FRS 27 basis. The realistic liability includes an assessment of the cost of any options and guarantees included in this business on a market consistent basis. The calculation has also taken account of bonus decisions which are consistent with the Principles and Practices of Financial Management. The shareholders' share of the future cost of bonuses is excluded from the assessment of the realistic liability.

Available capital resources - 2007

	With-profits 2007	UK other 2007	Ireland 2007	Life Business Shareholder Funds 2007	Total life business 2007	Other activities 2007	Group total 2007
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Shareholders' funds outside fund	–	–	–	25.0	25.0	25.3	50.3
Shareholders' funds held in fund	–	235.0	10.9	–	245.9	–	245.9
Total shareholders' funds	–	235.0	10.9	25.0	270.9	25.3	296.2
Adjustments onto regulatory basis:							
FFA	89.4	–	–	–	89.4	–	89.4
Adjustment to assets	22.8	(51.9)	(0.9)	–	(30.0)	(0.1)	(30.1)
Other adjustments	2.1	–	–	–	2.1	–	2.1
Other qualifying capital:							
Internal loans	25.0	–	–	(25.0)	–	–	–
Total available capital resources	139.3	183.1	10.0	-	332.4	25.2	357.6

Liability analysis - 2007

	With-profits	UK other	Irish	Total life business
	£m	**£m**	**£m**	**£m**
With-profits liabilities on realistic basis:				
Options and guarantees	97.6	–	–	97.6
Other policyholder obligations	878.6	–	–	878.6
Total with-profits liabilities	976.2	–	–	976.2
Unit-linked insurance contracts	–	538.1	63.8	601.9
Unit-linked investment contracts	–	697.1	112.7	809.8
Non-profit life assurance	–	369.5	29.0	398.5
Technical provisions in balance sheet	976.2	1,604.7	205.5	2,786.4

FRS 27, 45(a), (b)

The Group has a UK with-profits fund which is shown separately in the capital statement above. The Group's other UK life assurance business is shown in aggregate. The Irish life assurance business is also aggregated for the purposes of the statement.

For the Group's with-profits fund, the available capital is determined in accordance with the 'realistic balance sheet' regime prescribed by the FSA's regulations, under which liabilities to policyholders include both declared bonuses and the constructive obligation for future bonuses not yet declared. The available capital resources include an estimate of the value of the "estate", included as unallocated surplus. The estate represents the surplus in the fund that is in excess of any constructive obligation to policyholders. The allocation of the estate between policyholders and shareholders has not been determined. It represents capital resources of the with-profits fund and is available to meet regulatory and other solvency requirements of the fund and, in certain circumstances, additional liabilities that may arise. For the with-profits fund, the liabilities included in the balance sheet include only amounts relating to policyholders and do not include the amount representing the shareholders' share of future bonuses.

FRS 27, 42

Equity held outside the life funds and the equity in overseas businesses are shown separately in the capital statement. The capital requirements of the with-profits fund are met in part from centrally-held Group capital, by means of internal loans, contingent loans and share capital.

To the extent that this support is made under a formal arrangement, it is shown as an allocation of Group capital between the sections of the statement.

The total available capital resources for each section of the statement shows the capital on a realistic regulatory basis that is available to meet the regulatory capital requirements of that part of the business, and the targets for the surplus capital management regards as appropriate protection against future adverse changes in circumstances. Such capital is generally subject to restrictions as to its availability to meet requirements that arise elsewhere in the Group. The principal restrictions are:

(a) UK with-profits funds – the available surplus held in the fund can only be applied to meet the requirements of the fund itself or be distributed to policyholders and shareholders. Shareholders are entitled to an amount not exceeding one ninth of the amount distributed to policyholders in the form of bonuses, and the shareholders' share of distributions would also be subject to a tax charge.

(b) Other UK business – the available surplus held in the fund is attributable to shareholders and, subject to meeting the regulatory requirements of these businesses, this capital is available to meet requirements elsewhere in the Group. Any transfer of the surplus would give rise to a tax charge.

(c) Irish business – the available capital resources are subject to local regulatory restrictions which restrict management's ability to redeploy these amounts in other parts of the Group and such transfers would also give rise to a tax charge. Because of the nature of these restrictions, the Group's management does not regard this capital as available to meet requirements in other parts of the Group.

For the UK life funds the group is required to hold sufficient capital to meet the FSA capital requirements. For the with-profits fund this is based on the 'risk capital margin' (RCM) determined in accordance with the FSA's regulatory rules under its realistic capital regime. The determination of the RCM depends on various actuarial and other assumptions about potential changes in market prices, and the actions management would take in the event of particular adverse changes in market conditions. Consideration is also given to the Individual Capital Assessment (ICA) which takes into account certain business risks not reflected in the RCM.

Management intends to maintain surplus capital in excess of the RCM and ICA to meet the FSA's total requirements, and to maintain an appropriate additional margin over this to absorb changes in both capital and capital requirements. For the with-profits fund the capital was 152% of the RCM of £18.8 million, in line with management's target of maintaining capital of at least 150% of the RCM.

For UK non-profit business, the relevant capital requirement is the minimum solvency requirement determined in accordance with FSA regulations. For this business, a lower capital surplus is targeted by management, since the capital requirement is less subject to fluctuation and the capital amount is after deducting liabilities that include additional prudential margins. At 31 December 2008 the available capital was 145% of the capital requirement of £142.8 million, in excess of management's target minimum of 140%.

For the Irish business, the relevant capital requirement is the minimum requirement under the locally applicable regulatory regime. In practice the local regulator expects a significant margin over these minima to be maintained. Management also carries out its own assessment of the level of capital resources it regards as appropriate, in excess of these regulatory minima. Overall, the Irish business held capital substantially in excess of management's target minimum capital level of £7.4 million.

FRS 27, 55

Movements in capital resources

	With-profits	Other	Total
	£m	£m	£m
Balance at 1 January 2008	159.8	218.3	378.1
Effect of investment variations	3.1	1.8	4.9
Effect of changes in assumptions	23.2	49.3	72.5
Effect of changes in management policy	34.5	50.6	85.1
New business	(56.1)	(72.2)	(128.3)
Other factors	(0.7)	4.5	3.8
Balance at 31 December 2008	**163.8**	**252.3**	**416.1**

	With-profits	Other	Total
	£m	£m	£m
Balance at 1 January 2007	55.6	256.2	311.8
Effect of investment variations	2.0	2.8	4.8
Effect of changes in assumptions	6.1	7.3	13.4
Effect of changes in management policy	2.3	5.6	7.9
Effect of changes in regulatory requirements	135.2	-	135.2
New business	(41.7)	(58.1)	(99.8)
Other factors	0.3	4.5	4.8
Balance at 31 December 2007	**159.8**	**218.3**	**378.1**

FRS 27, 45(c)

Capital resource sensitivities

The capital position is sensitive to changes in market conditions, due to both changes in the value of the assets and the effect that changes in investment conditions may have on the value of the liabilities. It is also sensitive to assumptions and experience relating to mortality and morbidity and, to a lesser extent, expenses and persistency.

The most significant sensitivities arise from the following four risks:

- market risk in relation to the with-profits business, which would arise if adverse changes in the value of the assets supporting this business could not be fully reflected in payments to policyholders because of the effect of guarantees and options. The capital position of this business would also deteriorate if increases to the market cost of derivatives resulted in an increase in the liability for guarantees and options in the realistic balance sheet;
- mortality risk in relation to annuity business, which would arise if the mortality of annuitants improved more rapidly than the assumptions used for reserving;
- market risk in relation to annuity business, which would arise if the return from the fixed interest investments supporting this business were lower than that assumed for reserving; and
- mortality risk in relation to term assurance business, which would arise if mortality of the lives insured were heavier than that assumed, possibly because of an epidemic or catastrophe.

The timing of any impact on capital would depend on the interaction of past experience and assumptions about future experience. In general, if experience had deteriorated or was expected to deteriorate and management actions were not expected to reduce the future impact, then assumptions relating to future experience would be changed to reflect it. In this way, liabilities would be increased to anticipate the future impact of the worse experience with immediate impact on the capital position. Examples of possible management actions include changes to with-profits bonus rates and changes to discretionary surrender terms.

FRS 27 'Life assurance'

FRS 27, 30 — FRS 27 requires an entity to present quantitative and narrative disclosures of its regulatory capital position.

A statement of its total capital resources relating to each section of its long-term business is required, showing:

FRS 27, 32

(a) shareholders' funds (or in the case of a mutual, the equivalent, often described as disclosed surplus);
(b) adjustments to restate these amounts in accordance with regulatory requirements;
(c) each additional component of capital included for regulatory purposes, including capital retained within a life fund whether attributable to shareholders, policyholders or not yet allocated between shareholders and policyholders; and
(d) the total capital available to meet regulatory capital requirements.

FRS 27, 34 — The above statement should be analysed between:

(a) each UK with-profits life fund that is material to the group; and
(b) the entity's other life assurance business, showing the extent to which the various components of capital are subject to constraints such that they are available to meet requirements in only part of the entity's business, or are available to meet risks and regulatory capital requirements in all parts of the business.

FRS 27, 37 — The capital statement has to be reconciled to the shareholders' funds, FFA and other amounts shown in the entity's balance sheet, showing separately for each component of capital the amount relating to the entity's business other than life assurance. Where such other business is significant, an explanation shall be given of the extent to which this capital can be used to meet the requirements of the life assurance business.

FRS 27, 39, 42 — Where the reporting entity is a subsidiary undertaking, the capital statement shall explain the extent to which the capital of the entity is able to be transferred to the parent or fellow subsidiaries, or the extent to which it is required to be retained within the reporting entity. Any formal intra-group arrangements to provide capital to particular funds or business units, including intra-group loans and contingent arrangements, should also be disclosed.

PwC — The wording of the capital statement above is based on the example contained in Appendix I to FRS 27. In practice there may be a number of ways of presenting the capital position of a group. In particular, in the example wording in Appendix I to FRS 27, capital is expressed as being determined in accordance with the realistic balance sheet regime. However, in the Insurance Annual Return, capital is determined in accordance with the regulatory Pillar 1 regime, with the realistic regime impacting the calculation of the capital resources requirement but not the calculation of capital itself.

FRS 29 'Financial instruments: Disclosures'

FRS 29, E1, E2

Disclosures about an entity's capital are also required by FRS 29 'Financial Instruments: Disclosures' to enable users of its financial statements to evaluate its objectives, policies and processes for managing capital. This includes:

(a) qualitative information about its objectives, policies and processes for managing capital including:
  - a description of what it manages as capital;
  - any externally imposed capital requirements and how they are incorporated into the management of capital; and
  - how it is meeting its objectives;

(b) summary quantitative data about what it manages as capital;

(c) any changes from the previous period;

(d) whether it complied with any externally imposed capital requirements to which it is subject; and

(e) if it hasn't complied, the consequences of non-compliance.

2 Segmental analysis

SSAP 25

In the opinion of the directors, the Group operates in a single business segment, being that of long-term insurance business.

(a) *Gross premiums written*

Gross premium income is made up of:

		2008	2007
		£m	£m
Sch9A, 76(1)(a)	Direct insurance	**386.9**	363.8
Sch9A, 76(2)(a)	Reinsurance inwards	**15.1**	12.2
	Gross premiums written	**402.0**	376.0

		Regular premiums		Single premiums	
		2008	2007	2008	2007
		£m	£m	£m	£m
Sch9A, 76(2)(b)(ii), (iii)	**Gross direct premiums written in respect of insurance contracts and with-profits investment contracts**				
	Non-linked, non-profit:				
	Life	**20.3**	15.0	**35.2**	33.2
	Annuity	**3.1**	2.9	**2.9**	2.8
	Income protection	**4.5**	3.6	**–**	–
		27.9	21.5	**38.1**	36.0
	With-profits:				
	Pensions	**34.2**	33.7	**77.0**	73.3
	Life	**39.2**	36.6	**94.3**	91.7
		73.4	70.3	**171.3**	165.0
	Unit-linked insurance contracts:				
	Pensions	**12.6**	10.9	**24.1**	23.2
	Life	**11.8**	11.6	**27.7**	25.3
		24.4	22.5	**51.8**	48.5
	Total gross direct premiums written	**125.7**	114.3	**261.2**	249.5
	Comprising:				
Sch9A, 76(2)(b)(i)	- Individual business	**91.0**	85.3	**216.5**	208.6
	- Group contracts	**34.7**	29.0	**44.7**	40.9
		125.7	114.3	**261.2**	249.5

(b) *Gross new business premiums*

Gross new premium income is made up of:

ABI, 213

	2008	2007
	£m	**£m**
Direct insurance	**241.5**	223.4
Reinsurance inwards	**12.2**	10.1
Gross new business premiums	**253.7**	233.5

	Regular premiums		Single premiums	
	2008	**2007**	**2008**	**2007**
Gross new direct business premiums written	**£m**	**£m**	**£m**	**£m**
Non-linked, non-profit:				
Life	**3.6**	3.7	**35.2**	33.2
Annuity	**1.0**	0.9	**2.9**	2.8
Income protection	**1.5**	1.2	**–**	–
	6.1	5.8	**38.1**	36.0
With-profits:				
Pensions	**7.8**	6.9	**77.0**	73.3
Life	**11.5**	10.3	**94.3**	91.7
	19.3	17.2	**171.3**	165.0
Unit-linked insurance contracts:				
Pensions	**4.8**	3.5	**24.1**	23.2
Life	**3.6**	3.4	**27.7**	25.3
	8.4	6.9	**51.8**	48.5
	33.8	29.9	**261.2**	249.5
Comprising:				
- Individual business	**26.8**	24.1	**216.5**	208.6
- Group contracts	**7.0**	5.8	**44.7**	40.9
	33.8	29.9	**261.2**	249.5

In classifying new business premiums the following bases of recognition have been adopted:

- recurrent single premium contracts, including DWP rebates on certain pensions products, are included as new business, single premiums;
- increments under existing group pension schemes are classified as new business premiums;
- pensions vested into annuity contracts during the year are included as new annuity single premium business at the annuity purchase price; and
- products substituted due to the exercise of standard contract terms are not included in the new business statistics.

Where regular premiums are received other than annually, the reported regular new business premiums are on an annualised basis.

ABI, 214 The ABI SORP defines new business, quoting FSA rules, as follows:

'Single premium contracts shall consist of those contracts under which there is no expectation of continuing premiums being paid at regular intervals. Additional single premiums paid in respect of existing individual contracts shall be included.

Regular premium contracts shall include those contracts under which premiums are payable at regular intervals during the policy year, including repeated or recurrent single premiums where the level of premiums is defined.'

ABI, 215 Further FSA guidance is also quoted: 'It is typical of regular premium business that the office will issue a renewal notice for the expected amount of the premium, albeit that the policyholder may have a contractual right to pay a different amount, or nothing at all. Another characteristic might be that premiums collection is by direct debit or other payment order.'

ABI, 216 DSS rebates received on certain pensions contracts should be treated as single premiums. The Department of Social Security ('DSS') has since been incorporated into the Department for Work and Pensions ('DWP').

ABI, 217 Internal transfers between products where open market options are available should be counted as new business. If no open market option exists, the transfer should not be treated as new business.

(c) Geographical analysis

		Gross premiums written		Net assets		Profit before taxation	
		2008	**2007**	**2008**	**2007 (restated)**	**2008**	**2007 (restated)**
		£m	**£m**	**£m**	**£m**	**£m**	**£m**
	United Kingdom						
SSAP 25, 34 FRS 3, 15	Acquisitions	**48.1**	–	**29.3**	–	**3.5**	–
	Other continuing operations	**314.0**	339.8	**267.1**	269.1	**59.7**	64.1
		362.1	339.8	**296.4**	269.1	**63.2**	64.1
	Ireland						
Sch9A, 77(1)	Other continuing operations – direct insurance	**39.9**	36.2	**35.1**	33.1	**8.1**	6.7
		402.0	376.0	**331.5**	302.2	**71.3**	70.8
ABI, 308	Short-term fluctuations in investment returns					**10.0**	8.1
	As reported in the non-technical account					**81.3**	78.9

SSAP 25, 34 Gross premiums written by destination are not materially different from gross premiums written by source.

Of the gross premiums written in the United Kingdom, £347.0m (2007: £327.6m) relates to direct insurance.

(d) Reinsurance balance

Sch9A, 76(1)(b) The reinsurance balance amounted to a credit to the long-term business technical account at 31 December 2008 of £8.2m (2007: £10.3m).

Segmental Information

ABI, 220 The requirements for segmental analysis within the accounts of an insurance company or group are governed by Schedule 9A, the ABI SORP and SSAP 25 'Segmental Reporting'.

Schedule 9A Companies Act 1985

Sch9A, Pt II, 2(6) The disclosures required by Schedule 9A are strictly only required in individual entity accounts and not group accounts. They have been included here as an aid to users preparing individual entity accounts and as being indicative of the types of disclosure that may voluntarily be made in group accounts.

(a) analysis of gross premiums written by way of direct insurance and reinsurance

Sch9A, 76(3) Where reinsurance inwards business is undertaken, gross premiums written are required to be broken down between those written by way of direct insurance and those written by way of reinsurance. Such analysis is only required when either amount exceeds 10% of gross premiums written.

(b) analysis of premiums by type of contract

Gross direct premiums are required to be analysed between:

- individual premiums and premiums under group contracts;
- periodic premiums and single premiums; and
- premiums from non-profit contracts, premiums from with-profits contracts and premiums from contracts where the investment risk is borne by policyholders.

Sch9A, 76(3) Such analysis is only required if any amount exceeds 10% of gross premiums written by way of direct insurance.

(c) reinsurance balance

ABI, 264 Schedule 9A requires disclosure of the 'reinsurance balance'. This is defined in the ABI SORP as the aggregate total of all those items included in the technical account for long-term business which relate to reinsurance outwards transactions including reinsurance commissions and profit participations.

(d) analysis by geographical area

Where overseas business is conducted, a geographical analysis of gross direct premiums is required resulting from contracts concluded:

- in the EU member State of a company's head office;
- in other EU member States; and
- in other countries.

Sch9A, 77(2) The disclosure is only required where such amounts for each area exceed 5% of total gross premiums.

ABI SORP

ABI, 213 The ABI SORP expands on the requirements of Schedule 9A by recommending that segmental analysis should also be given for gross (and if materially different, net) new business premiums. In this regard, explanation of the basis adopted for recognising new annual and single premiums should be given. New annual premiums should be shown as the premiums payable in a full year.

PwC

The segmental disclosure requirements relating to premiums have been applied only to those contracts for which premiums are recorded within the long-term business technical account (i.e. insurance contracts and with-profits investment contracts). The disclosures do not include premiums in respect of unit-linked investment contracts which are subject to deposit accounting under FRS 26. If companies wish to include deposits received in respect of such contracts within their segmental disclosure it should be made clear that such amounts do not represent premiums as reported in the financial statements.

In the accounts of the Proforma-Life Group, the reinsurance of new business is not material.

SSAP 25 disclosures

SSAP 25, 34

SAAP 25 requires that turnover, the result before tax, minority interests and extraordinary items, and net assets be disclosed by class of business and by geographical segment.

SSAP 25, 30

A class of business is defined in SSAP 25 as 'a distinguishable component of an entity that provides a separate product or service or a separate group of related products or services'.

For the most part, insurance companies have interpreted this definition such that general insurance is taken to be one class of business and life assurance as another, with no additional analysis provided.

SSAP 25, 18

With regard to the geographical analysis, turnover should be disclosed by origin, i.e. the geographical area from which insurance contracts are supplied, and in addition by destination, i.e. the geographical location of risk, unless there is an immaterial difference between the two. Where this is the case, a statement to this effect will suffice.

ABI, 308

Where allocations of investment return have been made based on the longer-term rate of investment return, the ABI SORP requires the profit before tax of each segment shown in the segmental analysis to be based on the longer-term rate of investment return. The segmental results should then be reconciled to the total of the actual result before tax disclosed in the non-technical account.

SSAP 25, 26

FRS 9, 27

Where interests in associated undertakings form a significant part of a reporting entity's results or assets, the segmental analysis of profit and net assets is required to separately identify the amounts in respect of the interests in associated undertakings. Such an analysis in respect of turnover is only required where the reporting entity has taken up the option in FRS 9 to disclose its share of its associates' turnover as a memorandum item on the face of the profit and loss account.

For this purpose, associated undertakings are considered 'significant' if in total they account for at least 20% of the total result or 20% of the total net assets of the reporting entity.

Acquisitions and disposals

FRS 3, 15

FRS 6, 28

Where an acquisition, sale or termination has a material impact on a major business segment, the impact should be disclosed and explained.

3 Investment return

(a) Total investment return

		Long-term business technical account		Non-technical account	
		2008	**2007**	**2008**	**2007**
		£m	**£m**	**£m**	**£m**
	Investment income				
	Income from other financial investments:				
FRS 29, 20(a)(iii)	- Held-to-maturity interest income	**5.6**	4.9	**-**	-
FRS 29, 20(a)(iv)	- Loans and receivables interest income	**1.5**	1.4	**1.0**	0.8
FRS 29, 20(b)	Total interest income on financial assets not at fair value through profit or loss	**7.1**	6.3	**1.0**	0.8
	Income from financial assets at fair value through profit or loss	**84.3**	69.8	**-**	-
		91.4	76.1	**1.0**	0.8
	Income from associated undertakings	**4.2**	3.3	**-**	-
	Income from land and buildings	**10.8**	10.3	**-**	-
	Net return on pension scheme (Note 36)	**0.4**	0.5	**0.3**	0.4
	Net gains on the realisation of investments	**209.6**	164.6	**6.9**	-
		316.4	254.8	**8.2**	1.2
	Investment expenses and charges				
	Interest payable on financial liabilities, at amortised cost	**(1.3)**	(0.9)	**(5.3)**	(2.9)
	Other investment management expenses	**(6.9)**	(5.5)	**(0.2)**	(0.2)
	Net losses on the realisation of investments	-	-	-	(1.7)
	Total investment management expenses, including interest	**(8.2)**	(6.4)	**(5.5)**	(4.8)
	Net unrealised gains/ (losses) on investments	**173.5**	166.5	**(1.9)**	5.8
ABI, 230	Other finance income – net return on defined benefit pension scheme	**-**	**-**	**0.7**	0.9
	Total investment return	**481.7**	414.9	**1.5**	3.1
	Investment return is analysed between:				
	Investment return retained in the long-term business technical account / non-technical account	**471.7**	406.8	**11.5**	11.2
	Investment return allocated from the long-term business technical account to the non-technical account	**10.0**	8.1	**(10.0)**	(8.1)
	Total investment return	**481.7**	414.9	**1.5**	3.1
FRS 29, 20(a)(i)	Included in the total investment return are net gains or losses on financial assets at fair value through profit or loss:				
	Assets designated upon initial recognition	**363.5**	312.4	**3.5**	3.1
	Assets held for trading	**0.2**	0.1	**-**	-
	Total net realised and unrealised gains/(losses) included in investment return	**363.7**	312.5	**3.5**	3.1

		Long-term business technical account		Non-technical account	
		2008	2007	2008	2007
		£m	£m	£m	£m
	Interest expense for financial liabilities not at fair value through profit or loss comprises:				
	Interest payable on financial liabilities included in investment return above	**1.3**	0.9	**5.3**	2.9
	Interest expense in respect of unit-linked investment contracts	**150.8**	62.4	**-**	-
FRS 29, 20(a)(v)	Interest expense in respect of financial liabilities at amortised cost	**152.1**	63.3	**5.3**	2.9
	Interest expense in respect of with-profits investment contracts	**144.6**	97.5	**-**	-
FRS 29, 20(b)	**Total interest expense for financial liabilities not at fair value through profit or loss**	**296.7**	160.8	**5.3**	2.9

Interest expense relating to financial liabilities at amortised cost in respect of unit-linked investment contracts is included in the Technical account – Long-term business under the heading 'Change in other technical provisions'. See Note 30 'Technical provisions for linked liabilities'.

The interest expense in respect of with-profits contracts is calculated as the increase in the realistic liability for those contracts not attributable to amounts received from, or paid to, policyholders and is included within the Technical account – Long-term business under the heading 'Change in long-term business provision'.

FRS 29, 20

FRS 29 requires disclosure of the following items of income, expense, gains and losses either on the face of the financial statements or in the notes;

(a) net gains or net losses on:

- (i) financial assets or financial liabilities at fair value through profit or loss, showing separately those relating to assets designated upon initial recognition and those held for trading;
- (ii) available-for-sale assets;
- (iii) held-to-maturity investments;
- (iv) loans and receivables; and
- (v) financial liabilities at amortised cost;

FRS 29, 20A

(b) total interest income and total interest expense (calculated, except for contracts with a discretionary participation feature, using the effective interest method) for financial assets and liabilities not at fair value through profit or loss;

(c) fee income and expense (other than in (b) above) arising from assets or liabilities not at fair value through profit or loss and trust and fiduciary activities that result in the holding of assets on behalf of individuals, trusts, retirement benefit plans and other institutions;

(d) interest income on impaired financial assets; and

(e) the amount of any impairment loss for each class of financial asset.

(b) Longer-term investment return

ABI, 299 The longer-term investment return is calculated in respect of equity and property investments by applying the longer-term rate of return for each investment category to the quarterly weighted average of the corresponding assets, after adjusting for the effect of any short-term market movements.

ABI, 305 In respect of equities and properties the directors have determined the longer-term rates of investment return to be as follows:

	Longer-term rates of investment return	
	2008	**2007**
Equities – Sterling	**7.6%**	7.8%
– Euro	**6.1%**	6.2%
Properties	**8.7%**	8.7%

ABI, 303 The longer-term rate of investment return for fixed interest securities of 5.2% (2007: 5.5%) is calculated on the amortised cost basis with realised gains and losses subject to continuing amortisation over the remaining period to the maturity date.

ABI, 305 An increase/decrease of 1% in the longer-term rate of investment return would result in an increase/decrease in longer-term investment return reported in the technical account in respect of investments directly attributable to shareholders of £2.3m (2007: £2.0m).

ABI, 300
ABI, 301 Longer-term rates of investment return for equities and properties must be calculated separately. The calculations should use best estimates based on historic rates experienced and current inflation expectations. Consideration should be given to the business's actual returns over a period of not less than five years, to longer-term rates of return used by the business for other purposes (e.g. product pricing), to the rate used for the purpose of achieved profits reporting and to external expectations and influences. The rates thus determined should be reviewed at least annually although changes would be expected only infrequently.

PwC In practice, the setting of the longer-term rate of return is a subjective area, particularly in determining how much weight to give to historic performance and how much to current expectations.

PwC Judgement will also need to be exercised in assessing when deviations of actual investment return from the assumed longer-term rate indicate that the longer-term rate requires adjustment.

ABI, 303 The longer-term rate of return in respect of redeemable fixed interest securities may be determined either by using a redemption yield or on the amortised cost basis. In the case of irredeemable fixed interest securities and short-term assets, the longer-term investment return should be the interest income receivable in respect of the financial year.

ABI, 299 The allocation of investment return is calculated by applying the longer-term rate of investment return for each investment category to the quarterly weighted average of the corresponding assets. The allocation is adjusted to exclude the effect of any short-term market movements.

ABI, 299 The alternative method set out in the ABI SORP of calculating the transfer of investment return for equities and properties is to gross up actual investment income by a factor representing the longer-term rate of investment return divided by an assumed longer-term dividend or rental yield (making adjustments for any special factors which have distorted the underlying yield of the portfolio).

If this method is adopted, the assumed long-term rates of dividend yield or rental yield should be disclosed.

(c) Comparison of longer-term investment returns with actual returns

ABI, 305

	2004-2008	2003-2007
	£m	£m
Actual return attributable to shareholders from the long-term business	**134.0**	102.8
Longer-term return credited to operating results from the long-term business	**117.0**	106.4
Excess/(shortage) of actual returns over longer-term returns	**17.0**	(3.6)

ABI, 305

The ABI SORP requires a comparison over a period of not less than five years of actual return against the return determined using the longer-term rate of return.

4 Bonuses

ABI, 187

The aggregate of the bonuses added to policies in the year was £156.1m (2007: £141.6m).

5 Financial reinsurance

ABI, 262

On 1 July 2004, the Group entered into a reinsurance arrangement to assist in the financing of the acquisition costs of new long-term business. This contract does not transfer significant insurance risk and is accounted for as an investment contract. The net amount of the financing outstanding of £9.6m (2007: £9.8m) from the reinsurance arrangement is included within 'Other financial investments – Loans and receivables' and is carried at amortised cost in the balance sheet. Interest payable of £0.6m (2007: £0.6m) has been reflected in the long-term business technical account in respect of this contract.

The detailed requirements of the ABI SORP in respect of long-term reinsurance transactions are commented upon in the related accounting policy note. The ABI SORP states that the presentations and disclosure of reinsurance contracts should be such as to enable a clear understanding of their effect on the results.

Financial reinsurance contracts that principally transfer financial risk and do not transfer significant insurance risk will fall to be accounted for as investment contracts under FRS 26.

6 Net operating expenses

	2008	2007
	£m	£m
Acquisition costs	**50.8**	46.1
Change in deferred acquisition costs	**(17.8)**	(11.1)
Administrative expenses	**42.9**	30.7
Reinsurance commissions and profit participation	**(0.7)**	(0.5)
	75.2	65.2

ABI, 221

Long-term business levies

Levies raised by the Financial Services Compensation Scheme should be included within administrative expenses. The requirements regarding providing for such levies are discussed in the commentary to Note 31 'Provisions for other risks and charges'.

Sch9A, 78

Total commissions for direct insurance accounted for by the Group during the year, amounted to £13.2m (2007: £12.3m).

Sch9A, Pt II, 2(6)

The disclosure of total commissions for direct insurance is strictly only required in individual entity accounts, but is included here for illustrative purposes.

ABI, 218

The amount should exclude any commissions payable to employees.

Exchange differences of £2.5m (2007: £ (0.6) m) have been credited/(charged) to administrative expenses.

FRS 23, 52(a)

The amount of exchange differences recognised in profit or loss should be disclosed (except those arising on financial instruments measured at 'fair value through profit or loss' under FRS 26).

7 Auditors' remuneration

ICAEW Tech 06/06
SI 2005/2417 (Revised)

During the year the group (including its overseas subsidiaries) obtained the following services from the Company's auditor and its associates at costs as detailed below:

	2008	2007
	£'000	£'000
Audit services		
Fees payable to the Company's auditor for the audit of the Parent Company and consolidated accounts	**480**	350
Non-audit services		
Fees payable to the Company's auditor and its associates for other services:		
Audit of the Company's subsidiaries, pursuant to legislation	**80**	65
Other services pursuant to legislation, including the audit of the regulatory return	**40**	30
Tax services	**10**	
Compliance services	**10**	–
Advisory services	**10**	–
Other services not covered above	**10**	8
	640	453

	2008	2007
	£'000	£'000
Fees in respect of the Proforma-Life Limited pension scheme:		
Audit	**43**	42
Other services pursuant to legislation	**12**	11
	55	53

SI 2005/2417

The requirements in the Companies (Disclosure of Auditor Remuneration) Regulations 2005 on disclosure of auditor remuneration, apply to all financial statements with the following exceptions:

- Where a parent company is required to (and does) prepare consolidated financial statements, there is no requirement to disclose, in addition to the group audit fee, the audit fee for the company.

- The disclosures in respect of fees for ‘Other services’ are not required to be given by:
  - small or medium companies or groups (reduced disclosure requirements apply);
  - subsidiary companies in their individual financial statements, whose parents are required to, and do, prepare consolidated financial statements in accordance with the Companies Act 1985 and the subsidiary company is included in the consolidation; or
  - parent companies in their individual financial statements, where the company is required to, and does, prepare consolidated financial statements in accordance with the Companies Act 1985.

The statutory requirements in relation to auditors’ remuneration are supported by guidance published by the ICAEW in Tech 06/06 (Revised) “Disclosure of Auditors’ Remuneration” , which also provides example disclosures.

Disclosure is required of:

- any remuneration receivable by the company's auditors for the auditing of the accounts (parent company and group accounts); and
- any remuneration receivable by the company’s auditors or “its associates” for the supply of other services to the company or “its associates”.

Separate disclosure is required in the parent company’s group and individual financial statements in respect of fees paid to the ‘Auditor and its associates’ by the ‘Company and its associates’ (including that of countries and territories outside Great Britain) in the following categories:

- fees payable for the audit of the group financial statements (including the audit of the company’s subsidiaries for consolidation purposes only); and
- fees for other services including:
  - Audit of company’s subsidiaries (excluding consolidation work);
  - other services supplied pursuant to legislation;
  - other services relating taxation;
  - services relating to information technology;
  - internal audit services;
  - valuation and actuarial services;
  - services relating to litigation;
  - services relating to recruitment and remuneration;
  - services relating to corporate finance transactions entered into or proposed to be entered into by or on behalf of the company or any of its associates; and
  - all other services.

Separate disclosure is required of:

- fees in respect of the company and its subsidiaries; and
- fees in respect of company pension schemes.

The ‘Company and its associates’ refers to the subsidiaries of the company, and not to its associates as defined in FRS 9, ‘Associates and joint ventures’. Similarly, references to the ‘Auditor and its associates’ refer to members of the same network of firms as the company’s auditor.

Where fees for services performed by other parts of the audit firm that assist in the audit are invoiced either as part of, or separately from, the audit fee, then those fees are included within the audit fees disclosed.

The above disclosure requirements will still apply to parent company's individual financial statements where it chooses to take advantage of s228A Companies Act 1985 exemption from consolidation for intermediate holding companies within a group headed by a non-EEA parent company (where the accounts are drawn up in accordance with the Insurance Accounts Directive or in an equivalent manner).

8 Operating lease rentals

SSAP 21, 55

	2008	2007
	£m	**£m**
Plant and machinery	**0.3**	0.2
Other	**1.1**	0.9
	1.4	1.1

9 Staff costs

s231A(4)

Group	2008	2007
	£m	**£m**
Wages and salaries	**15.9**	14.8
Social security costs	**1.6**	1.5
Other pension costs	**2.4**	2.2
	19.9	18.5

s231A(1)

The average number of employees of the Group (including executive directors) during the year was as follows:

	2008	2007
	No.	**No.**
Administration and finance	**425**	398
Marketing	**243**	231
Investment	**26**	24
	694	653

The Company has no employees.

Employee numbers

s231A(5)

The Companies Act requires the categories for the purpose of the analysis of the average number of employees to be determined by the directors having regard to the manner in which the company's activities are organised.

FRS 20 'Share-based payment'

FRS 20 applies to all share-based payment transactions, which fall into three broad types:

- equity-settled share-based payment transactions – Transactions in which an entity receives goods or services, including employee services, as consideration for its own equity instruments. Such transactions include employee share option and share incentive plans;
- cash-settled share-based payment transactions – Transactions in which an entity acquires goods or services by incurring liabilities (typically to be settled in cash), but where the amount paid is based on the value of the entity's shares or other equity instruments. Typical examples include 'phantom' share schemes, share appreciation rights and certain long-term incentive schemes; and

- transactions in which either party may choose settlement in the form of cash (or other assets) or equity instruments of the entity.

Recognition of share-based payment transactions

The goods or services acquired in a share-based payment transaction should be recognised when they are received. For an equity-settled transaction, the corresponding entry will be within equity (shareholders' funds). For cash-settled transactions a liability will be recognised.

Measurement of equity-settled share-based payment transactions

The measurement objective of FRS 20 is to determine the fair value of the goods or services acquired by an entity. If the fair value of goods and services cannot be measured reliably, it should be measured indirectly by reference to the fair value of the equity instruments granted in consideration.

Vesting conditions

Vesting conditions are conditions that must be satisfied before a counterparty becomes unconditionally entitled to the equity instruments or payment to which they relate. Where equity instruments vest immediately, in the absence of evidence to the contrary, an entity should presume that they represent consideration for goods already received or services already rendered. In this case, on the date on which the options are granted the entity should recognise the goods or services received in full. However, if there is a specified period of service over which an award vests, the goods or services should be recognised over that vesting period.

Cash-settled share-based payment transactions

Expenses in respect of cash-settled share-based payment transactions should be recognised over the period during which goods are received or services are rendered and measured at the fair value of the liability. The fair value of the liability should be re-measured at each reporting date until settled, with changes in fair value recognised in the profit and loss account. Unlike equity-settled share-based payment transactions, the credit entry in respect of a cash-settled share-based payment transaction is presented as a liability.

Share-based payment transactions with alternative methods of settlement

Sometimes either the reporting entity or the counterparty has a choice as to whether to settle a share-based payment transaction in cash or with an issue of equity instruments.

Where the counterparty has the choice of settlement method, the standard concludes that the reporting entity has issued a compound financial instrument, comprising a debt component (the counterparty's right to demand payment in cash) and an equity component (the counterparty's right to demand settlement in equity instruments). There are detailed rules on the valuation and subsequent treatment of the instrument's debt and equity parts.

Where the reporting entity has the choice, the transaction should be treated as cash-settled if the option to settle in equity is not substantive or if the entity has a past practice or a stated policy of settling in cash. Otherwise, the transaction should be treated as equity-settled. Adjustments will then be necessary if the chosen method of settlement does not match the method of accounting.

Share-based payment arrangements involving equity instruments of the parent

UITF 44

UITF 44 was issued in February 2007 and its adoption is mandatory for financial periods beginning on or after 1 March 2007. UITF 44 implements IFRIC 11, ' IFRS 2 – Group and treasury share transactions', for UK GAAP reporters.

UITF 44 provides guidance on how to account for share-based payment arrangements that involve two or more entities within the same group. For example, where employees of a subsidiary are granted rights to equity instruments of its parent as consideration for the services provided to the subsidiary.

The accounting for such share-based payment arrangements hinges around which entity grants the award and therefore has the obligation to settle. When a parent entity grants rights over the parent's equity instruments to the employees of its subsidiary, as long as the share-based payment arrangement is accounted for as equity-settled in the consolidated financial statements, the subsidiary should treat the arrangement as an equity-settled arrangement (with the other side of the FRS 20 being a credit to equity that is not subject to subsequent remeasurement. Conversely, where a subsidiary grants rights over the parent's equity instruments to the subsidiary's employees, the subsidiary is required to account for the transaction as cash-settled and will, therefore, recognise a liability (re-measured at each balance sheet date) as the other side of the FRS 20 charge.

Disclosures

The standard requires extensive disclosure under three broad headings:

- the nature and extent of share-based payment arrangements that existed during the period;
- how the fair value of the goods or services received, or the fair value of the equity instruments granted during the period, was determined; and
- the effect of expenses arising from share-based payment transactions on the entity's profit or loss for the period.

UITF 38

Employee share ownership plans and similar arrangements

FRS 20 deals only with the expense of share-based payments and not with the accounting for assets and liabilities of employee share ownership plans. Guidance exists instead in UITF Abstract 38 'Accounting for ESOP trusts', which provides that where an entity has de facto control of an ESOP trust, certain of the ESOP's assets and liabilities should be brought back onto the entity's balance sheet. This is on the basis that, for all practical purposes, the sponsoring entity is in the same position as if it had purchased the shares directly and, therefore, should account for them in a similar way.

UITF 32

The UITF applied similar principles when it considered other arrangements involving employee benefit trusts. The resultant guidance in UITF Abstract 32, 'Employee benefit trusts and other intermediate payment arrangements', requires that when an entity transfers funds to an intermediary, there should be a rebuttable presumption that the sponsoring entity has exchanged one asset for another and that the payment itself does not represent an immediate expense. Hence, as for an ESOP trust, an employee benefit trust is treated as if it was an extension of the reporting entity itself.

Proforma-Life Limited has no share-based payments under FRS 20.

10 Directors' emoluments

		2008	2007
		£'000	**£'000**
Sch6, 1(1)(a)	Aggregate emoluments	**703**	542
Sch6, 1(1)(c)	Aggregate amounts receivable (excluding shares) under long-term incentive schemes	**213**	192
Sch6, 8(1)	Compensation for loss of office	**–**	50
Sch6, 9(1)	Sums paid to third parties for directors' services	**20**	18
	Excess retirement benefits		
Sch6, 7(1)(a)	- current directors	**20**	15
Sch6, 7(1)(b)	- past directors	**15**	10
		971	827

Sch6, 1(1)(e)

Retirement benefits are accruing to all of the directors under the Group's defined benefit pension scheme.

Highest paid director

		2008	2007
		£'000	**£'000**
Sch6, 2(1)(a)	Aggregate emoluments and amounts (excluding shares) receivable under long-term incentive schemes	**205**	189
Sch6, 2(2)	Defined benefit pension scheme:		
	- accrued pension at end of year (per annum)	**103**	98

Sch6, 1 (2)(b) Where applicable, the number of directors who exercised share options in the year and the number of directors who have become entitled to receive shares under any long-term incentive schemes are required to be disclosed.

Sch6, 2(1) The highest paid director disclosures are only required to be given where the aggregate of directors' emoluments and benefits under long-term incentive schemes exceeds £200,000.

Sch6, 2(2)(b) If the highest paid director is entitled to a lump sum payment on attaining normal pensionable age, the amount accrued at the balance sheet date is required to be disclosed.

11 Other technical income, net of reinsurance

Other technical income of £27.5m (2007: £25.3m) comprises fees for policy administration and asset management services arising from unit-linked investment contracts and relates to financial liabilities carried at amortised cost.

12 Other income and other charges

Non-technical account	2008	2007
	£m	**£m**
Other income comprises:		
Income arising from OEIC and investment management activity	**12.9**	12.4
Other operating income	**0.4**	0.3
	13.3	12.7
Other charges comprise:		
Expenses of OEIC and investment management activity	**8.9**	8.4
Amortisation of goodwill	**1.0**	–
Other operating charges	**0.5**	0.1
	10.4	8.5

13 Profit on ordinary activities before tax

As a result of the acquisition of ABC Insurance Company Limited, the following amounts have been charged to the profit and loss account in the current year:

		Long-term business technical account 2008	Non-technical account 2008
		£m	**£m**
	Administrative expenses:		
Sch9A, 80(3) FRS 7, 39	Reorganisation costs (see below)	**5.1**	–
	Other technical charges:		
	Amortisation of present value of acquired in-force business	**0.9**	–
	Other charges:		
	Amortisation of goodwill	**–**	1.0

Reorganisation costs

FRS 7, 39
Sch9A, 80(3)

The costs incurred in reorganising the business of ABC Insurance Company Limited arise from the relocation and integration of its pensions division with that of XYZ Insurance Company Limited. The costs relate to the project identified and controlled by management as part of the integration programme set up at the time of ABC Insurance Company Limited's acquisition.

14 Taxation

		2008	2007
FRS 16, 17		**£m**	**£m**
Sch9A, 74(1)	**Long-term business technical account**		
	UK corporation tax:		
	- Current tax on income for the period	**24.8**	22.0
	- Adjustments in respect of prior periods	**(1.4)**	(0.2)
		23.4	21.8
Sch9A, 74(3)	Double taxation relief	**(0.7)**	(0.6)
		22.7	21.2
	Foreign tax – Current tax on income for the period	**1.5**	1.2
	Total current tax	**24.2**	22.4
	Deferred tax:		
FRS 19, 60(a)(i)	- Origination and reversal of timing differences	**19.8**	5.1
FRS 19, 60(a)(i)	- Impact of change in UK tax rate	**(2.3)**	-
FRS 19, 60(a)(ii)	- Increase in discount	**(3.4)**	(1.2)
	Total deferred tax	**14.1**	3.9
	Tax on profit on ordinary activities	**38.3**	26.3

UK corporation tax in the technical account has been calculated at rates between 20% and 30% (2007: 20% and 28.5%) in accordance with the rates applicable to the long-term business of a long-term assurance company.

FRS 16, 17		2008	2007
		£m	£m
	Non-technical account		
Sch9A, 74(1)	UK corporation tax at 28.5% (2007: 30%)		
	- Current tax on income for the period	**1.5**	1.1
	- Adjustments in respect of prior periods	**0.2**	0.3
		1.7	1.4
Sch9A, 74(3)	Foreign tax – Current tax on income for the period	**0.1**	0.2
		1.8	1.6
	Tax attributable to allocated investment income	**2.8**	2.3
	Tax attributable to balance on long-term business technical account	**19.9**	17.3
FRS 9, 27	Share of taxation of associated undertaking	**1.2**	1.0
	Current tax charge for the period	**25.7**	22.2
	Deferred tax:		
FRS 19, 60(a)(i)	- Origination and reversal of timing differences	**0.2**	–
FRS 19, 60(a)(ii)	- Increase in discount	**–**	0.1
	Total deferred tax	**0.2**	0.1
	Tax on profit on ordinary activities	**25.9**	22.3

Factors affecting the tax charge for the period

FRS 19, 16

The tax assessed for the year is lower than the standard rate of corporation tax in the UK (28.5%). The differences are explained below:

		2008	2007 (restated)
		£m	£m
FRS 19, 64(a)	**Non-technical account**		
	Profit on ordinary activities before tax	**81.3**	78.9
	Profit on ordinary activities multiplied by standard rate of corporate tax in the UK of 28.5% (2007: 30%)	**23.2**	23.7
	Difference between effective and standard tax rate on balance on long-term business technical account	**1.5**	(1.5)
	Expenses not deductible for tax purposes	**0.7**	0.2
	Higher tax rates on overseas earnings	**0.2**	0.1
	Adjustments to tax charge in respect of previous periods	**0.1**	(0.3)
	Current tax charge for the period	**25.7**	22.2

FRS 19, 64

Companies are required to provide a reconciliation between the current tax charge or credit on ordinary activities reported in the profit and loss account to the current tax charge that would result from applying a relevant standard rate of tax to the profit on ordinary activities before tax. This reconciliation may be of either the monetary amounts or the rates (as a percentage of profit on ordinary activities before tax) and should only apply to the tax borne by shareholders through the non-technical account.

Particulars should be provided of any special circumstances which affect the liability in respect of taxation of profits, income or capital gains for the current or succeeding financial years.

15 Dividends on equity shares

	2008	2007
	£m	**£m**
Ordinary shares		
2008 Interim: 5p (2007: 5p) per 25p share	**8.8**	8.8
2007 Final: 6.5p (2006: 6.25p) per 25p share	**11.4**	11.4
	20.2	20.2

FRS 21, 13

In addition, the directors are proposing a final dividend in respect of the financial year ended 31 December 2008 of 8.5p per share, which will absorb an estimated £15.0m of shareholders' funds.

16 Goodwill - Group

Sch9A, 62
FRS 10, 53

	2008
	£m
Cost	
At 1 January 2008	**–**
Acquisition during year	**30.1**
At 31 December 2008	**30.1**
Amortisation	
At 1 January 2008 (Sch9A, 33 & 62(3))	**–**
Charge for the year	**(1.0)**
At 31 December 2008	**(1.0)**
Net book value at 31 December 2008	**29.1**
Net book value at 31 December 2007	–

FRS 10, 55
Sch9A, 36

The directors have assessed the useful economic life of the goodwill arising on the acquisition of ABC Insurance Company Limited as 15 years, based on the period over which the value of the underlying business acquired is expected to exceed the values of the acquired identifiable net assets.

FRS 10, 71(a)

The cumulative amount of goodwill (net of goodwill attributable to subsequent disposals) eliminated against reserves in respect of acquisitions made prior to 1998 is £22.1m (2007: £22.1m).

Amortisation of goodwill

FRRP PN58

Neither the ABI SORP nor Schedule 9A offer any guidance as to where in the profit and loss account the amortisation of goodwill should be recognised. It is clear, however, following reaffirmation by the FRRP in January 2000 that the amortisation should be charged as part of operating profit.

PwC

In these illustrative accounts, the amortisation of goodwill arising on the acquisition of ABC Insurance Company Limited (a life insurance company) by the shareholders of Proforma-Life Limited has been charged to 'Other charges' in the non-technical account. In practice, recognition of the charge in 'Other technical charges' in the long-term business technical account would also be acceptable.

PwC

In all of the situations contemplated above, the amortisation is charged in arriving at profit before tax which is commonly regarded by insurers as equating to operating profit.

17 Acquisition

FRS 6, 21, 24

On 7 July 2008 Proforma-Life Limited acquired the whole of the issued share capital of ABC Insurance Company Limited for a cash consideration of £94.6m. The company transacts life assurance and pensions business. The Group has used acquisition accounting to account for the purchase.

Acquired assets and liabilities, fair value adjustments and goodwill

		Book value of net assets on acquisition	Revaluations	Accounting policy realignment	Fair values of net assets on acquisition
		£m	£m	£m	£m
FRS 6, 25	**Assets**				
	Investments				
	- financial assets	136.1	–	–	**136.1**
	Present value of in-force long-term business (see Note 21)	–	39.9	–	**39.9**
	Assets held to cover linked liabilities	110.1	–	–	**110.1**
	Other assets	12.8	–	(0.5)	**12.3**
	Long-term business provision and claims outstanding	(104.1)	–	–	**(104.1)**
	Technical provisions for linked liabilities	(104.5)	–	–	**(104.5)**
	Fund for future appropriations	(14.1)	–	–	**(14.1)**
	Other liabilities	(10.3)	–	–	**(10.3)**
	Net assets acquired	26.0	39.9	(0.5)	**65.4**
FRS 6, 24	**Cash consideration** (including £0.9m of acquisition costs)				**95.5**
Sch4A, 13(3)	**Goodwill**				**30.1**

The adjustment in respect of 'other assets' represents the write-off of capitalised computer software costs in line with the Group's policy of charging all such costs as an expense when incurred.

The present value of in-force long-term business represents the fair value of the estimated shareholders' interest in future surpluses expected to emerge from business in-force of the acquired subsidiary.

FRS 6, 36
Sch4A, 13(4)

In its last financial year to 31 December 2007, ABC Insurance Company Limited made a profit after tax of £8.6m. There were no transactions between the Proforma-Life Group and the acquired subsidiary prior to the date of acquisition. For the period from that date to the effective date of acquisition, the summarised profit and loss account for ABC Insurance Company Limited is set out below.

	Period from 1 January 2008 to 6 July 2008
	£m
Long-term business technical account	
Gross written premiums	**45.2**
Non-technical account	
Profit before tax	**6.8**
Tax	**(2.1)**
Profit after tax	**4.7**

ABC Insurance Company Limited had no recognised gains or losses other than the profit for the period.

A summarised profit and loss account and statement of total recognised gains and losses of the acquired entity for the period from the beginning of its financial year to the effective date of acquisition is required when:

- the fair value of the consideration given exceeds 15% of the net assets of the acquiring entity; and
- the net assets or operating profits of the acquired entity exceed 15% of those of the acquiring entity.

The information should be shown on the basis of the acquired entity's accounting policies prior to the acquisition.

Impact of the acquisition on the current year's results

	Acquisition	Other continuing operations	Total
	£m	£m	£m
Long-term business technical account			
Earned premiums, net of reinsurance	47.1	338.8	385.9
Investment income	10.1	306.3	316.4
FRS 6, 28 Unrealised gains on investments	13.1	160.4	173.5
Other technical income	2.2	25.3	27.5
Claims incurred, net of reinsurance	(40.1)	(402.1)	(442.2)
Change in other technical provisions, net of reinsurance	(12.2)	(261.9)	(274.1)
Net operating expenses	(12.1)	(63.1)	(75.2)
Investment expenses and charges	(0.3)	(7.9)	(8.2)
Other technical charges – including amortisation of present value of in-force business	(0.9)	(1.2)	(2.1)
Tax attributable to the long-term business	(3.4)	(34.9)	(38.3)
Allocated investment return transferred to the non-technical account	(0.5)	(9.5)	(10.0)
Change in present value of future profits on non-profit business written out of the with-profits fund	–	4.5	4.5
Actuarial loss on pension scheme	–	(0.2)	(0.2)
Transfers to the fund for future appropriations	(0.2)	(9.6)	(9.8)
Balance on Technical account – Long-term business	2.8	44.9	47.7
Non-technical account			
Balance on Technical account – Long-term business (pre-tax)	3.9	63.7	67.6
Investment income	0.1	4.1	4.2
Unrealised gains on investments	0.1	2.0	2.1
Allocated investment return transferred from the long-term business technical account	0.5	9.5	10.0
Investment expenses and charges	(0.1)	(5.4)	(5.5)
Other income	–	13.3	13.3
Other charges – including amortisation of goodwill	(1.0)	(9.4)	(10.4)
Operating profit	3.5	77.8	81.3

PwC

In the year of acquisition it is appropriate that any amortisation of goodwill arising on the acquisition should be attributed to the results of the acquisition. This reflects the fact that the amortisation is a cost of making the acquisition and from a group perspective is therefore a cost attributable to the acquired business. In the following year both the results and amortisation of goodwill should be reclassified in the comparatives as continuing operations. Similar considerations apply to the amortisation of the present value of acquired in-force business.

18 Land and buildings - Group

	2008	2007
	£m	**£m**
Freehold	**137.8**	131.9
Long leasehold	**42.5**	40.2
	180.3	172.1

Sch9A, 28

The purchase price of land and buildings was £166.7m (2007: £165.1m).

Sch9A, BS(4)

Included in land and buildings at market value is £33.5m (2007: £32.4m) in respect of land and buildings occupied by the Group for its own use.

Sch9A, 63

Land and buildings were valued at 31 December 2008 on an open market existing-use basis (and at market value based on vacant possession for owner-occupied properties) by Capability & Brown, a firm of independent Chartered Surveyors.

Bank borrowings are secured on freehold land and buildings to a value of £2.4m (2007: £3.7m) (Note 32 'Financial liabilities').

19 Investments in group undertakings and participating interests

(a) Investments in participating interests – Group

	Carrying Value		Cost	
	2008	2007	2008	2007
	£m	**£m**	**£m**	**£m**
Investment in associated undertaking	**40.1**	38.2	**19.1**	19.1

FRS 9, 52
Sch5, 22
Sch9A, 28

The Group has an investment in an associate company, Associate 1 Limited, a company incorporated in Great Britain and whose principal activity is the undertaking of life assurance business. The Group holds 30% of the nominal value of the allotted ordinary shares of Associate 1 Limited. The interest is held by a wholly-owned subsidiary undertaking of Proforma-Life Limited.

FRS 9, 57, 58

Certain additional disclosures are required by FRS 9 in circumstances where the investor's aggregate share in its associates exceeds 15% of any of the gross assets, gross liabilities, turnover or, on a three-year average, operating result of the investing group. The disclosures are further extended if any of the above exceeds 25% of the balance of the group's equivalent amount.

FRS 9, 55

The Proforma-Life Group does not have any balances outstanding with its associated undertaking at the balance sheet date. Where there are any amounts owing or owed between an investor and its associates or joint ventures these should be analysed between amounts relating to loans and amounts relating to trading balances. This disclosure may be combined with those required by FRS 8 'Related Party Disclosures'.

SSAP 25, 36

SSAP 25 requires certain segmental analysis in relation to associates where they comprise more than 20% of the group's total assets or result.

(b) Investments in group undertakings - Company

	Shares in Group undertakings	Loans to Group undertakings	Total
	£m	**£m**	**£m**
At 1 January 2008	235.1	31.3	266.4
Acquisition	95.5	-	95.5
Repayment of loan	-	(10.0)	(10.0)
At 31 December 2008	**330.6**	**21.3**	**351.9**

Sch5, 15, 16

Set out below are the Company's investments in subsidiary undertakings as at 31 December 2008, all of which are included in the consolidation. All the companies are incorporated in Great Britain, unless otherwise indicated. An asterisk* indicates holdings held directly by the Company. The shares held are voting ordinary equity shares.

Name of undertaking	Principal activity	Percentage of nominal value and voting rights
XYZ Insurance Company Limited	Life assurance and pensions	100*
ABC Insurance Company Limited	Life assurance and pensions	100*
Proforma-Life Mutual Fund Management Limited	OEIC management	100
Proforma-Life Ireland Company Ltd (Ireland)	Life assurance and pensions	82
Proforma-Life Asset Management Ltd	Investment management	100
Proforma-Life Management Services	Limited Management services	100

FRS 28, 11(d)

Corresponding amounts are not required to be disclosed in respect of details of shareholdings in subsidiary undertakings held by a company or, where group accounts are prepared, held by the parent company and by the Group.

20 Other financial investments – Group

FRS 29, 8

Financial assets	Carrying value 2008 £m	Carrying value 2007 £m	Cost 2008 £m	Cost 2007 £m
Financial assets at fair value through profit or loss				
Designated upon initial recognition	**3,130.3**	2,617.8	**2,230.5**	1,735.4
Derivative financial instruments - held for trading	**2.1**	1.8	**2.0**	1.9
	3,132.4	2,619.6	**2,232.5**	1,737.3
Held to maturity, at amortised cost (Sch9A, 24(6))	**112.1**	96.0	**87.6**	101.9
Loans and receivables, at amortised cost	**88.4**	99.2	**87.9**	98.6
Total financial assets	**3,332.9**	2,814.8	**2,408.0**	1,937.8
Included in balance sheet as follows:				
Other financial investments (Sch9A, PL)				
Shares and other variable-yield securities and units in unit trusts	**1,259.3**	988.2	**935.3**	675.7
Debt securities and other fixed income securities	**322.3**	311.5	**251.2**	212.1
Loans secured by mortgages	**20.1**	16.3	**20.1**	16.3
Other loans:	**26.3**	19.5	**26.3**	19.5
Deposits with credit institutions	**31.6**	53.2	**31.6**	53.2
Other, including financial reinsurance contract (Note 5)	**10.4**	10.2	**10.4**	10.2
	1,670.0	1,398.9	**1,274.9**	987.0
Assets held to cover linked liabilities (see Note 22)	**1,662.9**	1,415.9	**1,133.1**	950.8
Total financial assets	**3,332.9**	2,814.8	**2,408.0**	1,937.8

FRS 29, 8

FRS 29 requires the carrying amounts of each of the following categories, as defined in FRS 26, to be disclosed either on the face of the balance sheet or in the notes:

(a) financial assets at fair value through profit or loss, showing separately (i) those designated as such upon initial recognition and (ii) those classified as held for trading in accordance with FRS 26;

(b) held-to-maturity investments;

(c) loans and receivables;

(d) available-for-sale financial assets;

(e) financial liabilities at fair value through profit or loss, showing separately (i) those designated as such upon initial recognition and (ii) those classified as held for trading in accordance with FRS 26 (see Note 32); and

(f) financial liabilities measured at amortised cost (see Note 32).

Proforma-Life limited has no financial assets designated as “available-for-sale”.

FRS 29, 12

If an entity reclassifies a financial asset between ‘at fair value’ and ‘at cost or amortised cost’, the amounts reclassified and the reason for the reclassification should be disclosed.

FRS 29, 15

Where an entity holds collateral of financial or non-financial assets and is permitted to sell or re-pledge the collateral in the absence of default by the owner of the collateral, the fair value of the collateral held should be disclosed, together with the fair value of any collateral sold or pledged and whether the entity has an obligation to return it and also the terms and conditions associated with its use of the collateral.

(a) Listed investments

Sch9A, 65

Included in the carrying values of other financial investments above are amounts in respect of listed investments as follows:

	2008	2007
	£m	**£m**
Shares and other variable-yield securities and units in unit trusts	**898.8**	715.5
Debt securities and other fixed-income securities	**314.3**	300.4
	1,213.1	1,015.9

(b) Financial assets at amortised cost

Sch9A, 24

Those debt securities and other fixed-income securities that are held to maturity are valued at amortised cost. The fair value of these securities was £124.8m (2007: £106.5). For those debt securities and other fixed-income securities valued at amortised cost where the maturity value exceeded purchase price, the unamortised difference at the year-end was £18.4m (2007: £10.2m); where the purchase price exceeded the maturity value, the difference was £Nil (2007: £0.4m). The fair value is based on market prices or broker/dealer price quotations. Where this information is not available, fair value has been estimated using quoted market prices for securities with similar credit, maturity and yield characteristics.

FRS 29, 29(a)

For loans and receivables at amortised cost the carrying value is a reasonable approximation of fair value.

FRS 29, 20(d)&(e)

At the reporting date, there were no assets held at amortised cost that were either impaired or overdue.

(c) Other loans

Sch9A, PL(7)

Included within other loans are loans secured on policies with a cost and carrying value of £18.2m (2007: £15.1m).

(d) Assets valued using a valuation technique

The Group closely monitors the valuation of assets in markets that have become less liquid. Determining whether a market is active requires the exercise of judgement and is determined based upon the facts and circumstances of the market for the instrument being measured. Where it is determined that there is no active market, fair value is established using a valuation technique as described in Accounting Policy I above. The techniques applied incorporate relevant information available and reflect appropriate adjustments for credit and liquidity risks. The relative weightings given to differing sources of information and the determination of non-observable inputs to valuation models can require the exercise of significant judgement.

For corporate bonds for which there is no active market the fair value is based on broker/dealer price quotations. Where possible the Group seeks at least two quotations for each bond and considers whether these are representative of fair value in light of current traded levels. Where this information is not available or where it is considered to be not representative of fair value, fair value has been estimated using quoted market prices for securities with similar credit, maturity and yield characteristics.

The £37m (2007 £52m) fair value of certain asset backed securities has been determined by use of an internal model which predicts the future cashflows from the instruments in a number of projected economic scenarios. These economic scenarios are probability weighted based on recent economic forecasts and the resulting cash flows are discounted using risk adjusted discount rates determined by reference to currently observable market discount rates adjusted to take account of the risk characteristics of the securities being valued. There is significant subjectivity in this valuation as there is little recent market activity in these or other similar instruments. Reasonably possible alternative assumptions used in respect of these securities could increase or decrease fair values by £6 million (2007 increase or decrease £1m). The total amount of changes in fair values in respect of such instruments recognised in profit and loss was a decrease of £11m (2007 increase £1m).

Fair values

FRS 29, 25, 27 The fair value of each class of financial assets and financial liabilities should be disclosed, together with the methods used in determining fair values (whether in whole or in part, directly by reference to published price quotations in an active market or estimated using a valuation technique). If a valuation technique is used the following additional disclosures are necessary:

FRS 29, 27(a), (c)
(i) the assumptions adopted and whether the valuation technique is based on assumptions not supported by prices from observable current market transactions in the same instrument or observable market data; and
(ii) where fair values are recognised in the financial statements, if changing one or more of those assumptions to reasonably possible alternative assumptions would change fair value significantly, the entity shall state this fact and disclose the effect of those changes. For this purpose, significance shall be judged with respect to profit or loss, and total assets or total liabilities, or, when changes in fair value are recognised in equity, total equity.

FRS 29, 27(d) If (i) or (ii) above apply the total amount of the change in fair value estimated using such a valuation technique that was recognised in profit or loss during the period should be disclosed.

FRS 29, 29 Disclosures of fair value are not required;

(a) when the carrying amount is a reasonable approximation of fair value, for example, for financial instruments such as short-term trade receivables and payables;
(b) for an investment in equity instruments that do not have a quoted market price in an active market, or derivatives linked to such equity instruments, that is measured at cost in accordance with FRS 26 because its fair value cannot be measured reliably; or
(c) for a contract containing a discretionary participation feature if the fair value of that feature cannot be measured reliably.

FRS 29, 30 In the cases described in (b) and (c) above, information is required to help users of the financial statements make their own judgements about the extent of possible differences between the carrying amount of those financial assets or financial liabilities and their fair value, including:

(a) the fact that fair value information has not been disclosed for these instruments because their fair value cannot be measured reliably;
(b) a description of the financial instruments, their carrying amount, and an explanation of why fair value cannot be measured reliably;
(c) information about the market for the instruments;
(d) information about whether and how the entity intends to dispose of the financial instruments; and
(e) if financial instruments whose fair value previously could not be reliably measured are derecognised, that fact, their carrying amount at the time of derecognition, and the amount of gain or loss recognised. Debt securities and other fixed-income securities.

Amortised cost

ABI, 284 Where debt and other fixed-income securities are carried at amortised cost, disclosure is required of the aggregate totals of purchase price, amortised cost and current value, together with the net excess/deficit of the amounts repayable at maturity over the carrying value.

Sch9A, 65C(2) Where the market value of investments held at amortised cost is less than the carrying value, it is necessary to explain why the carrying value had not been impaired. This is not applicable for Proforma-Life Limited.

Loans secured by mortgages

Sch9A BS(7) Loans secured by mortgages should be shown as such even where they are also secured by insurance policies.

Sch9A BS(7) **Other loans**

Loans to policyholders, for which the policy is the main security, are required to be included under ‘Other loans’ and their amount should be separately disclosed in the notes to the financial statements. Where the amount of

‘Other loans’ not secured by policies is material, an appropriate analysis is required to be given in the notes to the financial statements.

Deposits with credit institutions

Sch9A BS(8) Where sums deposited are subject to a time restriction on withdrawal, they should be included under ‘deposits with credit institutions’. Where no such restriction is in force, even where the amounts bear interest, they should be included in ‘cash at bank and in hand’.

Other investments

Sch9A BS(9) ‘Other’ investments should comprise those investments which may not sensibly be included in the other investment categories of the balance sheet format. Where such amounts are significant they should be separately disclosed in the notes to the financial statements.

Market volatility

PwC The last year has seen significant volatility in financial markets across the globe, initially triggered by rising defaults in the US sub-prime markets. However, these initial defaults have led to a broader ‘financial markets crisis, involving a widespread shortage of liquidity and a general widening of credit spreads, extending far beyond the US sub-prime market in which the initial issues arose. There has been the collapse of a number of significant financial institutions with others requiring public sector support.

There has been activity by accounting standard setters in response to the market volatility with the IASB looking to act on recommendations made earlier in the year by the Financial Stability Forum in the areas of off balance sheet vehicles, fair value in illiquid markets and disclosure in financial statements. Amendments to international standards made or proposed by IASB can be expected to be replicated by the ASB in the corresponding UK standards.

In October 2008 IASB published guidance on the application of fair value measurements in illiquid markets and improvements to financial instruments disclosures and measurements (which have been mirrored in amendments to FRS 26 and FRS 29) as discussed in the commentary to accounting policy I to these financial statements: ‘Accounting policies’. In addition, an exposure draft of further amendments to IFRS7 (FRS29) has been published with a view to further enhance disclosures

However, there remain further areas where modifications to the existing accounting framework are being sought. Both the European Commission and the G20 group of world leaders have indicated areas where further changes to accounting standards should be considered. The IASB and FASB held a number of round table meetings in Autumn 2008 to gather to gather input on reporting issues arising from the global financial crisis. In addition, an international advisory group of senior leaders with broad international experience with financial markets is being formed. This group will consider how improvements in financial reporting could help enhance investor confidence in financial markets; and will identify the accounting issues requiring urgent and immediate attention of the IASB and FASB as well as issues for longer-term consideration.

Insurers will need to consider the impact of the current market conditions on their 2008 financial statements; in particular the impact on the following areas may be of relevance:

- Asset valuation

The market illiquidity has led to difficulties in establishing the fair value of some financial assets liabilities. Consideration needs to be given as to whether an active market exists for an instrument from which a quoted price can be sourced. Where there is no active market fair value may need to be established using a modelled “valuation technique”. The appropriateness of the valuation technique used and the model inputs will need careful consideration as their application could affect the asset valuation significantly.
The IASB’s October 2008 guidance on fair value in illiquid markets highlights that determining that a market is inactive requires judgement and that further significant judgement may be required to determine fair value in

such a market. However, the guidance emphasises that regardless of the valuation technique used, that technique should not ignore relevant information and reflects appropriate risk adjustments that market participants would require for credit and liquidity risk.
Consideration may also need to be given to the valuation of non-financial assets (eg commercial property) in light of market conditions.

- Financial asset classification

Insurers will need to perform any reclassifications of financial assets as permitted by the ASB's amendments to FRS 26 published in October 2008. It should be noted that assets that have been designated at fair value through profit and loss are not permitted to be reclassified.

- Impairment of financial assets

For financial assets not at fair value through profit and loss, the need to recognise impairments will need to be considered. Impairment issues may arise for directly affected assets (eg investments backed by securities with sub-prime exposures) and indirectly affected assets whose value has fallen due to general market conditions. In assessing impairments it is important that companies have a full understanding of the counterparties to which they are exposed.

- Guarantees and loan commitments

Companies that gave guarantees or loan commitments to entities affected by recent market events may need to consider the valuation of their obligations under those guarantees and commitments.

- Hedge ineffectiveness

Companies that utilise hedge accounting should be alert to the possibility that hedge ineffectiveness may result from recent market conditions.

- Embedded derivatives

The value of some previously immaterial embedded derivatives may have become material as a result of recent market events.

- Insurance liabilities

Actuarial reserves should appropriately reflect the increased credit spreads on debt instruments.

- Disclosure

Where there are risks or uncertainties surrounding the financial statements the inclusion of appropriate disclosures is a key element in ensuring that these factors are adequately understood by the users of the accounts. In considering the adequacy and appropriateness of disclosures preparers should give consideration to the overriding requirements for the financial statements to give a true and fair view and for the directors' report to give a description of the principal risks and uncertainties facing the company.

In addition, FRS 29 requires extensive and potentially complex disclosures in areas including:
- qualitative disclosures such as the exposures to risk arising from the financial instruments;
- quantitative disclosures such as summary data about the exposures at the reporting date, and
- market risk information such as a sensitivity analysis for each type of market risk to which the entity is exposed at the reporting date, showing how profit or loss and equity would have been affected by changes in the relevant risk variable that were reasonably possible at that date.

In making such disclosure insurers will need to consider their particular circumstances, for example considering the extent to which counterparty exposures (including exposures arising through stock-lending or derivative transactions) or liquidity risks require specific mention.

For some insurers regulatory capital may have been significantly adversely impacted by market conditions and consideration should be given to how this should be reflected in the regulatory capital disclosures given under IAS 1 (and, for life insurers, any capital statement prepared in accordance with FRS 27). Consideration may also need to be given to going concern disclosures in circumstance where the impact of market volatility related issues raises any doubts over the appropriateness of the going concern assumption.

In considering the extent and nature of such disclosures each insurer will need to consider the facts and circumstances that are relevant to it, taking into account the materiality of the matters concerned.

21 Present value of acquired in-force business - Group

	2008
	£m
Cost	
At 1 January 2008	–
Acquisition during year	39.9
At 31 December 2008	**39.9**
Amortisation	
At 1 January 2008	–
Amortisation during year	0.9
At 31 December 2008	**0.9**
Net book value at 31 December 2008	**39.0**
Net book value at 31 December 2007	–

ABI, 191

We have commented on the accounting treatment of the acquired value of in-force business under the relevant accounting policy note. The ABI SORP requires that the PVIF asset and the amortisation for the accounting period should be disclosed separately. As noted in that commentary, we have interpreted amortisation in this context to comprise amortisation and the unwind of the discount taken together.

22 Assets held to cover linked liabilities – Group

Sch9A 28(3)

	Carrying value		**Cost**	
	2008	**2007**	**2008**	**2007**
	£m	**£m**	**£m**	**£m**
Assets held to cover unit-linked insurance contracts	**691.6**	604.9	**472.7**	415.5
Assets held to cover unit-linked investment contracts	**971.3**	811.0	**660.4**	555.3
	1,662.9	1,415.9	**1,133.1**	970.8

Assets held to cover linked liabilities are stated gross of £9.3m (2007: £4.2m), relating to linked fund investments in the process of settlement, which is included within ‘Creditors arising out of direct insurance operations’.

An analysis of total financial assets, including assets held to cover linked liabilities is provided in Note 20 ‘Other financial investments’.

Derivative financial instruments, at fair value through profit or loss, held for trading

Sch9A, 29A

Included within assets held to cover linked liabilities are forward currency contracts with a fair value of £2.1m (2007: £1.8m) that cost £2.0m (2007: £1.9m). All of these contracts are listed on recognised exchanges and so the quoted price is regarded as fair value. Cash flows under these contracts are dependent upon the exchange rates prevailing at the dates on which the contracts mature. Movements in fair value arise due to variations in exchange rates and are reflected in the profit and loss account. Fair value gains included in profit for the year amounted to £0.2m (2007: loss of £0.3m).

PwC

The balance sheet heading 'Assets held to cover linked liabilities' should be used for assets backing linked investment contracts, accounted for under FRS 26, as well as assets backing any linked insurance contracts.

PwC

In these illustrative financial statements, assets held to cover linked liabilities have been disclosed gross of any associated creditor balances, with the liabilities of the linked funds being disclosed in the appropriate caption on the liability side of the balance sheet. In practice a number of companies disclose a net figure for linked assets in order that the figure equates to the amount disclosed under technical provisions for linked liabilities (net of reinsurers' share). There are merits to both approaches in that whilst the former is consistent with the requirements of FRS 5, the latter acknowledges the presumed objective of the balance sheet format of showing the 'ring-fenced' nature of the linked funds as a whole as compared to the liabilities to policyholders.

ABI, 191

Where net assets held to cover linked liabilities differ significantly from the technical provisions for linked liabilities, disclosure should be made of the reasons for any significant mismatching. The ABI SORP clarifies that in practice this should apply only to overseas companies included in group financial statements.

Derivatives

Sch9A, 65A

Where the fair value accounting rules have been used to value derivatives, Schedule 9A requires the following disclosures:

- the basis of the valuation adopted;
- the purchase price;
- the assumptions used in valuation techniques;
- the fair value and movements recorded in the profit and loss; and

Sch9A, 65B

- for each class of derivatives, the extent and nature of the instrument, including significant terms and conditions that may affect the amount, timing and uncertainty of future cash flows.

23 Debtors arising out of direct insurance operations - Group

	2008	2007
	£m	**£m**
Due from policyholders	**20.1**	9.2
Due from intermediaries	**25.4**	8.1
	45.5	17.3

Sch9A BS(13)

Amounts owed by group undertakings and undertakings in which the company or group has a participating interest are required to be shown separately as sub items of 'Debtors arising out of direct insurance operations', 'Debtors arising out of reinsurance operations' and 'Other debtors'.

24 Tangible assets – Group

Sch9A, 33, 62(3)

	Motor vehicles	Computer equipment	Fixtures, fittings and office equipment	Total
Cost	**£m**	**£m**	**£m**	**£m**
At 1 January 2008	4.9	13.7	4.4	23.0
Additions	1.5	5.5	0.3	7.3
Disposals	(1.6)	(2.4)	(0.1)	(4.1)
At 31 December 2008	**4.8**	**16.8**	**4.6**	**26.2**
Sch9A, 33,62(3) **Depreciation**				
At 1 January 2008	3.0	8.1	1.8	12.9
FRS 15, 100(c) Charge for the year	1.2	4.7	0.4	6.3
Eliminations in respect of disposals	(1.4)	(1.8)	(0.1)	(3.3)
FRS 15, 100(f) **At 31 December 2008**	**2.8**	**11.0**	**2.1**	**15.9**
FRS 15, 100(h) **Net book value at 31 December 2008**	**2.0**	**5.8**	**2.5**	**10.3**
Net book value at 31 December 2007	1.9	5.6	2.6	10.1

Sch9A, 33(2) The charge for depreciation for the year ended 31 December 2007 was £6.1m.

FRS 15, 100(d) If material, the financial effect of a change in estimated useful economic lives or residual values should be disclosed.

FRS 15, 102 Where there has been a change in the method of depreciation, any material effect should be disclosed in the period of change. The reason for the change should also be disclosed.

In the table above, the amounts included within the 'additions' line arising from the Group's acquisition of ABC Insurance Company Limited during the year are not material. Where such amounts are more significant, we consider it best practice to separately analyse that part of 'additions' arising from acquisitions.

FRS 28, 11(a) Corresponding amounts are not required to be disclosed in relation to details of additions, disposals, revaluations, transfers and cumulative depreciation of fixed assets.

25 Deferred acquisition costs - Group

	2008	2007
	£m	**£m**
On insurance contracts and with-profits investment contracts	**68.8**	51.6
On non-profit investment contracts	**8.8**	8.2
	77.6	59.8

26 Assets attributable to the long-term business funds

Sch9A, 10(2) Total assets include £3,591.3m (2007: £3,056.5m) attributable to the long-term business funds of the Group's subsidiary companies.

Sch9A, Pt II, 2(2) This disclosure is strictly only required in respect of single entity balance sheets prepared in accordance with Schedule 9A, but is given here for illustrative purposes.

27 Share capital

Reference		Group and Company 2008	Group and Company 2007
		£m	£m
Sch9A, 58 (1)(a),(b)	**Authorised:**		
	240m (2007: 240m) ordinary shares of 25p each	**60.0**	60.0
	6.0m 7% (2007: 6.0m) cumulative preference shares of £1 each	**6.0**	6.0
		66.0	66.0
	Allotted and fully paid:		
	176.0m (2007: 176.0m) ordinary shares of 25p each	**44.0**	44.0
	6.0m 7% (2007: 6.0m) cumulative preference shares of £1 each	**6.0**	6.0

Sch9A, 58(2) The 7% cumulative preference shares, which do not carry any voting rights, are redeemable at par, at the Company's discretion, on or before 1 July 2014. Shareholders are entitled to receive dividends at 7% per annum on the par value of these shares on a cumulative basis; these dividends are payable on 31 December each year. On winding up, the preference shareholders rank above ordinary shareholders and are entitled to receive £1 per share and any dividends accrued but unpaid in respect of their shares.

FRS 25, 18(a) Preference shares are included within financial liabilities.

PwC The disclosures regarding authorised and allotted share capital required by paragraph 58 of Schedule 9A will include all legal share capital, regardless of how the shares are classified for accounting purposes.

28 Share premium account and reserves

Reference		Share premium account	Profit and loss account
	Group	**£m**	**£m**
	Balance at 1 January 2008, as previously reported	**55.8**	**197.0**
	Prior year adjustment		
	- Amendment to FRS 17 – valuation of listed securities'	-	**(0.6)**
	Balance at 1 January 2008, as restated	**55.8**	**196.4**
	Retained profit for the financial year	-	**53.5**
	Dividends paid on equity shares	-	**(20.2)**
FRS 23, 32	Exchange movements	-	**2.1**
FRS 17, 57	Actuarial loss on pension scheme	-	**(0.1)**
	Balance at 31 December 2008	**55.8**	**231.7**

	Share premium account	Profit and loss account
Company	**£m**	**£m**
Balance at 1 January 2008	**55.8**	**153.5**
Retained profit for the financial year	**-**	**42.0**
Dividends paid on equity shares	**-**	**(20.2)**
Balance at 31 December 2008	**55.8**	**175.3**

Sch9A, 66

Movements in reserves and provisions

Schedule 9A requires an analysis to be given of the movements in reserves and provisions. The disclosure applies only to items included within the balance sheet liability category "provisions for other risks and charges" and does not include movements in technical provisions.

FRS 28, 11(b)

Corresponding amounts are not required to be disclosed in respect of transfers to or from reserves and provisions and the source and application of any transfers.

Profit for the financial year

s230

As permitted by s230 CA85, the Company's profit and loss account has not been included in these financial statements. The Company's profit for the financial year was £42.0m (2007: £36.7m).

29 Long-term business provision - Group

Asset shares within the realistic liabilities for with-profits contracts have been determined in line with our Principles and Practice of Financial Management (PPFM).

The cost of options and guarantees in the long-term business provision in respect of with-profits business is calculated using a stochastic model (see Accounting policy P 'Long-term business provision'). The principal demographic assumptions in this calculation are as follows:

	Persistency %		Mortality	
Class of business	**2008**	**2007**	**2008**	**2007**
With-profits endowments	**7.5**	7.5	**AM92 ult**	AM92 ult
With-profits deferred annuities	**5.0**	5.0	**AM92 ult**	AM92 ult

Significant assumptions in the stochastic model are investment volatility and correlations between the returns on different asset classes. Asset expected returns and volatilities have been calibrated to ensure consistency with market values at an appropriate term for our anticipated liability profile. The equity volatility is assumed to be 25% and the property volatility is 15%. The cost of guarantees will be higher with higher investment volatility. The correlation assumptions have been based on management's view of the interaction between returns on different asset classes over the last 10 years; the correlations are assumed to be:

(i) 25% between equities and gilts;
(ii) 20% between equities and property; and
(iii) 10% between gilts and property.

FRS 27, 20
FRS 27, 48(c)
FRS 27, 51

Options and guarantees

For options and guarantees not falling within the scope of the FSA realistic capital regime, insurers are encouraged, but not required, to adopt stochastic modelling techniques. Where such options and guarantees are not measured at fair value or at an amount estimated using a market-consistent stochastic model, information about exposures to interest rate risk or market risk must be given including;

(a) a description of the nature and extent of the options and guarantees;

(b) the basis of measurement for the amount at which these options and guarantees are stated, and the extent to which an amount is included for the additional payment that may arise under the option or guarantee in excess of the amounts expected to be paid under the relevant policies if they did not include the option or guarantee feature;

(c) the main variables that determine the amount payable under the option or guarantee; and

(d) information on the potential effects of adverse changes in those market conditions that affect the entity's obligations under options and guarantees.

All Proforma-Life's options and guarantees are valued using stochastic methods.

PwC

Present value of non-profit business written out of the with-profits fund

Depending upon the materiality of the balance, it may be appropriate to disclose the significant assumptions underlying the calculation of the present value of non-profit business written out of the with-profits fund.

INS PRU 1.3.141R
GN 45, 3.3.3.2

Planned enhancements

The FSA's realistic liabilities must include any future planned enhancements to policyholder benefits. Actuarial guidance (GN45) published in 2005 indicates that for a closed with-profits fund, it would normally be expected that the whole of any inherited estate would be distributed over time and that, in such a situation, planned enhancements would be recognised in respect of the general intention to distribute the estate, and this would result in realistic liabilities being increased so that the working capital becomes, by definition, zero. Under FRS 27, the realistic liabilities recorded within the long-term business provision include such planned enhancements with a corresponding reduction of the FFA.

In calculating realistic liabilities, account has also been taken of future management actions consistent with those set out in our PPFM. The most significant of these are changes to the equity backing ratio depending on market conditions, bonus assumptions and changes to policy asset shares in market stress scenarios.

PwC

The management actions included within an insurer's PPFM will depend upon the company's specific circumstances and will lead to different impacts on the realistic liabilities.

The principal assumptions underlying the calculation of the long-term business provision in respect of non-profit business are as follows:

Sch9A, 46(2)

	Lapse rate % p.a.		**Mortality**		**Interest rate %**	
Class of business	**2008**	**2007**	**2008**	**2007**	**2008**	**2007**
Term assurances	**10.0**	9.0	**TM92 ult**	TM92 ult	**4**	3.75
Annuities in payment	**0.0**	0.0	**90% PMA00 mc (min underpin 1.7% p.a)**	PMA92lc (min underpin 1.7% p.a)	**5.50**	5.25

For female lives, the equivalent female life table is used.

ABI, 184

The long-term business provision allows for any future valuation strain. To the extent that recurring single premiums are paid under a with-profits deferred annuity contract, provided the terms of the payment of those single premiums are not fixed contractually, then no future allowance will be made. Sufficient assets are allocated to cover future strain where it is determined that this will arise.

A prudent assessment was made of lapse and withdrawal rates in calculating the liabilities for non-profit contracts.

PwC

The appropriate assumptions in respect of lapses will be dependent on the nature and mix of an insurer's business and on whether the mathematical reserves for a given contract are positive or negative. There may be a correlation between persistency and certain financial assumptions which should be disclosed. Any allowance for potential take-up of guaranteed rates under guaranteed annuity options should be disclosed.

ABI, 184

Assumptions are set by reference to publicly available market data and then validating that the current assumptions continue to reflect actual experience.

An increase in lapses on with-profits business reduces the cost of guarantees, as fewer policy holders remain to receive the guaranteed benefits. Lower lapses, or an increase in persistency, increase the cost of guarantees. A 1% increase in persistency on this business would result in an increase in the long-term business provision of approximately £14m.

An increase in lapses on term assurance business reduces the long-term business provision, as fewer deaths are expected when fewer policyholders remain in force. A 1% decrease in lapses on this business would result in an increase in the long-term business provision of approximately £1m.

A reduction in interest rates would reduce the impact of discounting on the long-term business provision, resulting in an increased provision. If, for example, the valuation interest rate were to be reduced by 0.5%, the long-term business provision would increase by approximately £70m. This does not include the corresponding effect on the valuation of assets.

If a lower mortality rate were assumed to apply, the long-term business provision would increase in respect of annuities and decrease in respect of assurances. A 5% reduction in mortality would increase the liabilities for annuities by approximately £2 million and decrease the liability for assurances by approximately £1 million.

The level of expenses included in the valuation is set at a risk group level and is based on the current year's expenses allowing for cost inflation of 3.5% per annum.

Proforma-Life has not made disclosure of morbidity assumptions, as these are not significant for the classes of business written. They would be significant for insurers writing significant PHI or critical illness business.

FRS 18, 55(d)

The principal changes to assumptions made since the previous accounting period and the related effects are as follows:

- an increase in the interest rates used reflecting the change in interest yields on backing assets – reducing the long-term business provision and increasing profit before tax by £8.5m (profit after tax by £5.9m);
- a strengthening of the mortality basis used for annuities in payment to reflect increasing longevity – increasing the long-term business provision and reducing profit before tax by £9.0m (profit after tax by £6.2m); and
- an increase in the lapse rate used for term assurance business to reflect lower persistency – reducing the long-term business provision and increasing profit before tax by £1.2m (profit after tax by £0.8m).

Material change to an estimation technique

FRS 18, 55(d)
FRS 18, 57

Where the effect of a change to an estimation technique is material, FRS 18 requires disclosure of the change and, where practicable, the effect on the results for the period.

The description of a significant estimation technique will include details of those underlying assumptions to which the monetary amount at which an item is to be measured is particularly sensitive. We note that this does not necessarily mean that the effect of changes in assumptions needs to be disclosed if there is no change in the estimation technique. Yet other standards may require it. The ABI SORP currently contains no such requirement, although in our view, where the effect of a change in assumption is significant it has always been best practice to disclose its impact and the reason for the change.

With-profits investment contracts

FRS 29, 30

Included within the long-term business provision are amounts of £382.5m (2007: £331.7m) relating to liabilities under with-profits investment contracts, where there is no transfer of significant insurance risk. These investment contracts contain a discretionary participation feature which entitles the holder to receive, as a supplement to the guaranteed benefits, additional benefits or bonuses through participation in the surplus arising from the assets held in the investment with-profits fund. These supplemental discretionary returns are subject to the discretion of the Group. The Group has the discretion within the constraints of the terms and conditions of the instrument, and UK regulations, to allocate part of the surplus to the contract holders and part to shareholders.

The Group cannot measure reliably the fair value of with-profits investment contracts due to the lack of a reliable basis to measure the supplemental discretionary returns and because there is not an active market for such instruments.

30 Technical provisions for linked liabilities - Group

	Unit-linked investment contracts		Unit-linked insurance contracts		Total	
	2008	**2007**	**2008**	**2007**	**2008**	**2007**
	£m	**£m**	**£m**	**£m**	**£m**	**£m**
At 1 January	**809.8**	718.4	**601.9**	563.0	**1,411.7**	1,281.4
Deposits received from policyholders under investment contracts	**90.4**	86.7	**-**	-	**90.4**	86.7
Acquisitions	**-**	-	**104.5**	-	**104.5**	-
Payments made to policyholders of, and fees deducted from, investment contracts	**(83.9)**	(57.7)	**-**	-	**(83.9)**	(57.7)
Change in technical provision as shown in the technical account	**150.8**	62.4	**(19.9)**	38.9	**130.9**	101.3
At 31 December	**967.1**	809.8	**686.5**	601.9	**1,653.6**	1,411.7

FRS 29, 25

Financial liabilities in respect of unit-linked investment contracts are carried in the balance sheet at amortised cost. The related fair value of these financial liabilities is £967.1m (2007: £809.8m), which is equivalent to the amount payable under the contract, based on the current fund value together with an allowance for any excess of future expenses over charges where appropriate. The return on the underlying assets is recorded as interest expense within Note 3 'Investment return'.

All movements in unit-linked insurance contracts, other than acquisitions and disposals, including premium receipts and claims payments, are recorded in the Technical account – Long-term business under the heading 'Change in technical provisions for linked liabilities'.

31 Provisions for other risks and charges – Group

FRS 12 'Provisions, contingent liabilities and contingent assets'

FRS 12, 3(c)
PwC
FRS 12, 3(d)

Insurance companies are exempt from the requirements of FRS 12 "Provisions, contingent liabilities and contingent assets" in respect of items arising from contracts with policyholders. As a result, an insurer's technical provisions will not be within the scope of FRS 12. In addition, we interpret this exemption to extend to balances in respect of the outwards reinsurance of contracts with policyholders and so, in particular, the reinsurers' share of technical provisions will not be within the scope of FRS 12. However, the requirements of FRS 12 will, in general, apply to balances shown under the heading "Provision for other risks and charges" except where they are covered by a more specific requirement of an FRS or an SSAP.

FRS 12, 14
FRS 12, 36

FRS 12 states provision should be made when and only when a company has a legal or constructive obligation at the balance sheet date, resulting from a past event, which it is probable will lead to a transfer of economic benefits which can be reliably estimated. The amount that should be provided should represent the best estimate of the expenditure required.

FRS 12, 89 & 90

In addition to an analysis of movements in provisions during the year, narrative disclosure should be given, for each class of provision, of the nature of the obligation giving rise to the provision and the expected timing of the transfer of economic benefit. Disclosure should also be made of uncertainties surrounding the quantum and timing of the transfer.

Refer also to the text box at the start of the Accounting policies section, which discusses the ABI SORP guidance on the application of FRS 12 to insurers in the context of FRS 18.

Sch9A, 66

	Deferred tax	Other	Total
	£m	£m	£m
At 1 January 2008	44.2	3.1	47.3
Charge for the year	14.3	2.2	16.5
Utilised in the year	–	(1.9)	(1.9)
At 31 December 2008	**58.5**	**3.4**	**61.9**

Deferred tax

FRS 19, 61(a)

The provision for deferred tax in the financial statements is as follows:

	2008	2007
	£m	£m
Deferred acquisition costs	**8.2**	6.5
Unrealised gains on investments	**64.4**	48.4
Short-term timing differences	**1.5**	1.0
Total deferred tax before discount	**74.1**	55.9
Discount (FRS 19, 61(b))	**(15.6)**	(11.7)
Total deferred tax after discount	**58.5**	44.2

FRS 19, 64

Deferred Tax

FRS 19 FRS 19 'Deferred tax' requires full provision to be made for deferred tax assets and liabilities arising from timing differences between the recognition of gains and losses in the financial statements and their recognition in a tax computation.

The general principle underlying the requirements is that deferred tax should be recognised as a liability or asset if the transactions or events that give the entity an obligation to pay more tax in future or a right to pay less tax in future have occurred by the balance sheet date.

The FRS:

(a) requires deferred tax to be recognised on most types of timing difference, including those attributable to:
- accelerated capital allowances;
- accruals for pension costs and other post-retirement benefits that will be deductible for tax purposes only when paid;
- elimination of unrealised intragroup profits on consolidation;
- unrelieved tax losses; and
- other sources of short-term timing differences;

(b) prohibits the recognition of deferred tax on timing differences arising when:
- a fixed asset is revalued without there being any commitment to sell the asset;
- the gain on sale of an asset is rolled over into replacement assets; and
- the remittance of a subsidiary, associate or joint venture's earnings would cause tax to be payable, but no commitment has been made to the remittance of the earnings; and

(c) requires deferred tax assets to be recognised to the extent that it is regarded as more likely than not that they will be recovered.

As an exception to the general requirement not to recognise deferred tax on revaluation gains and losses, the FRS requires deferred tax to be recognised when assets are continuously revalued to fair value, with changes in fair value being recognised in the profit and loss account.

The FRS permits but does not require entities to adopt a policy of discounting deferred tax assets and liabilities.

The FRS includes other requirements regarding the measurement and presentation of deferred tax assets and liabilities. These include requirements for the deferred tax to be:

- measured using tax rates that have been enacted or substantively enacted; and
- presented separately on the face of the balance sheet if the amounts are so material that, in the absence of such disclosure, readers may misinterpret the financial statements.

The FRS requires information to be disclosed about factors affecting current and future tax charges. A key element of this is a requirement to disclose a reconciliation of the current tax charge for the period to the charge that would arise if the profits reported in the financial statements were charged at a standard rate of tax. FRS 19 also amends FRS 7 'Fair values in acquisition accounting'. The amendment requires deferred tax recognised in a fair value exercise to be measured in accordance with the requirements of the FRS. Thus, deferred tax would not be recognised on an adjustment to recognise a non-monetary asset acquired with the business at its fair value on acquisition.

ABI, 188 Where the LTBP has been determined on an actuarial basis that has regard to the timing of tax relief where assumed expenses exceed attributable income, the insurer should ensure that such tax relief is excluded from the determination of any deferred tax requirement.

ABI, 189 Where the technical provisions for linked liabilities have regard to the timing of the tax obligation, the effect of this should be excluded from the determination of any deferred tax requirement.

ABI, 204 The deferred tax provision, including deferred tax provided in relation to unrealised investment gains, should be shown separately under 'Provisions for other risks and charges – Provision for taxation'. Any net deferred tax asset should be shown as a separate sub-heading within assets as 'Debtors – Other debtors'.

ABI, 205 Any policy to discount deferred tax should be applied to the whole of the insurer's business, including shareholders' interests.

ABI, 207 The ABI SORP deals with the specific instance where some element of the long-term fund is identified as being referable solely to shareholders. An example of this may be where there has been an attribution of the inherited estate which has been recognised as a shareholder profit in the modified statutory accounts but which has not been declared as surplus. In circumstances where the liability to pay tax is dependent on an event under the entity's control (such as the recognition of surplus) then, under the incremental liability approach followed by FRS 19, no event giving rise to the need to provide deferred tax has occurred, and so no additional deferred tax should be provided. Disclosure should be made of the amount of any deferred tax not recognised on such a timing difference determined using the anticipated incremental rate of tax (using enacted tax rates and legislation) assuming the existing basis of taxation is maintained.

Other provisions

Other provisions primarily relate to provisions for future premium levies anticipated to be raised during 2007.

Long-term business levies

ABI, 222 Provisions for premium levies should be made in accordance with FRS 12. The ABI SORP clarifies that the 'past event' which may give rise to an obligation in respect of premium levies is the recognition in the financial statements of the premium by reference to which the levy is calculated.

ABI, 223 Provision should be made for levies declared after the balance sheet date but prior to completion of the financial statements where the levy relates to premiums recognised at the balance sheet date. In addition, provision should be made for potential future levies based on premium income already recognised in the financial statements where it is assessed as more likely than not that a levy will be raised and where it is possible to make a reasonable estimate of the contingency. In this regard consideration may need to be given to any statement of intent by a guarantee fund to raise further levies, or any consistent trend in the amount and timing of levies in previous periods.

ABI, 222 Where the conditions for establishing a provision are not satisfied, consideration should be given to whether disclosure of a contingent liability is required.

ABI, 224 The ABI SORP confirms that it is appropriate to provide for levies related to future premium receipts (in respect of in-force business) within the long-term business provision, unless such levies can be charged against assets held to cover linked liabilities.

32 Financial liabilities at amortised cost

		Group		Company	
		2008	2007	2008	2007
		£m	£m	£m	£m
Sch9A, 68(1), (2)	**Debenture and other loans, repayable otherwise than by instalments (unsecured), at amortised cost**				
	In less than five years:				
	6.25% guaranteed bonds 2011	**32.5**	32.5	**32.5**	32.5
	In more than five years:				
	7.375% guaranteed bonds 2016	**20.0**	–	**20.0**	–
	6.0m 7% cumulative preference shares of £1 each	**6.0**	6.0	**6.0**	6.0
		58.5	38.5	**58.5**	38.5
Sch9A, 68(4)	**Amounts owed to credit institutions, at amortised cost**				
	Bank loans				
	- secured	**8.7**	14.4	**–**	–
	– unsecured	**30.3**	3.1	**29.1**	2.1
	Bank overdrafts	**15.1**	4.1	**10.2**	–
		54.1	21.6	**39.3**	2.1
	Total borrowings - financial liabilities at amortised cost	**112.6**	60.1	**97.8**	40.6
	Other financial liabilities, at amortised cost				
	Investment contract liabilities (included in Technical provisions for linked liabilities – see Note 30)	**967.1**	809.8	**-**	-
	Creditors	**78.7**	65.5	**25.8**	12.9
FRS 29, 8(f)	**Total financial liabilities, at amortised cost**	**1,158.4**	935.4	**123.6**	53.5

The bank loans at 31 December 2008 and 2007 are repayable within one year or on demand and are chargeable at various interest rates from 0.75% to 2.0% above LIBOR.

Sch9A, 68(4) The secured loans are secured as a first charge over the freehold properties of the companies concerned (see Note 18 'Land and buildings').

FRS 29, 29(a) The carrying amount of amounts owed to credit institutions approximate their fair value.

FRS 29, 25 The carrying amounts and fair value of the non-current borrowings are as follows:

	Carrying amounts		Fair values	
	2008	2007	2008	2007
	£m	£m	£m	£m
Debenture and other loans				
Guaranteed bonds 2011 and 2016	**52.5**	52.5	**46.6**	45.8
Redeemable preference shares	**6.0**	6.0	**5.6**	5.7
	58.5	58.5	**52.2**	51.5

The aggregate fair values of borrowings are determined using a discounted cash flow model, based on a current yield curve appropriate for the remaining term to maturity. The discount rate used in the valuation technique is based on the borrowing rate of 5.5% (2007: 5.2%).

The carrying amounts and fair value of unit-linked non-profit investment contract liabilities are shown in Note 30 'Technical provisions for linked liabilities'.

FRS 29, 31, 34(c)

The carrying amounts of the Group's borrowings are denominated in the following currencies:

	2008	2007
	£m	**£m**
UK Pounds	**108.9**	51.6
Euros	**3.7**	2.5
	112.6	54.1

Creditors

Sch9A, 68

The specific disclosure requirements of Schedule 9A in respect of each category shown under creditors in a company or group's balance sheet are as follows:

(a) the aggregate amount of debts which are payable or repayable otherwise than by instalments and fall due for payment or repayment after five years, together with debts which are payable or repayable by instalments, any of which fall due for payment or repayment after five years;

(b) the terms of payment or repayment and the rate of any interest payable in respect of debts falling within (a) above. (Where the directors are of the opinion that the number of debts would result in this disclosure being of excessive length, it is permissible to give a general indication of the term of payment or repayment and the rates of any interest payable on the debts);

(c) the aggregate amount of any debts in respect of which security has been given by the company and an indication of the nature of such securities so given;

(d) amounts owed by group undertakings or undertakings in which the group or company has a participating interest should be shown separately as sub-items.

Sch9A, BS (29)

In addition the amount of any convertible loans included within debenture loans are required to be disclosed separately.

FRS 29, 8

FRS 29 requires the carrying amounts of the following categories of financial liabilities, as defined in FRS 26, to be disclosed either on the face of the balance sheet or in the notes:

- financial liabilities at fair value through profit or loss, showing separately (i) those designated as such upon initial recognition and (ii) those classified as held for trading; and
- financial liabilities measured at amortised cost.

Proforma-Life Limited carries all financial liabilities at amortised cost.

FRS 29, 10

Where an entity has designated a financial liability as at fair value through profit or loss under FRS 26, it is required to disclose the following, together with the methods used:

(a) the amount of change, during the period and cumulatively, in the fair value of the financial liability that is attributable to changes in the credit risk of that liability determined either:

  (i) as the amount of change in its fair value that is not attributable to changes in market conditions that give rise to market risk (including benchmark interest rate, the price of another entity's financial instrument, a commodity price, a foreign exchange rate or an index of prices or rates. For contracts that include a unit- linking feature, changes in market conditions include changes in the performance of the related internal or external investment fund); or

  (ii) using an alternative method the entity believes more faithfully represents the amount of change in its fair value that is attributable to changes in the credit risk of the liability; and

(b) the difference between the financial liability's carrying amount and the amount the entity would be contractually required to pay at maturity to the holder of the obligation.

FRS 29, 11(b)

If the entity believes that the disclosure it has given to comply with the above requirements does not faithfully represent the change in the fair value of the financial asset or financial liability attributable to changes in its credit risk, the reasons for reaching this conclusion and the factors it believes are relevant should be disclosed.

FRS 29, 14 FRS 29 requires disclosure of the carrying amount of financial assets it has pledged as collateral for liabilities or contingent liabilities, together with the related terms and conditions.

FRS 29, 18 For loans payable at the reporting date, the following information should be given:

- details of any defaults during the period of principal plus interest, sinking fund or redemption terms on those loans;
- carrying amount of any loans in default at the balance sheet date; and
- whether the default was remedied or terms renegotiated before the financial statements were authorised for issue.

FRS 29, 19 The above disclosures also relate to other breaches of loan agreements which permitted the lender to demand accelerated repayment (unless remedied or renegotiated before the year end date).

33 Other creditors including tax and social security

		Group		Company	
		2008	**2007**	**2008**	**2007**
		£m	**£m**	**£m**	**£m**
SSAP 8, 14	Corporation tax	**30.3**	25.1	**4.1**	3.3
	Other creditors	**8.9**	3.3	**–**	–
		39.2	28.4	**4.1**	3.3

Sch9A, 68 Except as indicated in Note 32 'Financial liabilities', all creditors are payable within a period of five years.

34 Managed funds

Sch9A, 11(2) The following assets and liabilities of group pension funds administered by the Group in its own name but on behalf of others have been included in the consolidated balance sheet:

	2008	**2007**
	£m	**£m**
Land and buildings	**10.1**	5.2
Shares and other variable-yield securities and units in unit trusts	**90.2**	97.2
Debt securities and other fixed-income securities	**87.9**	63.5
	188.2	165.9
Cash at bank and in hand	**3.2**	4.2
Debtors	**1.4**	1.3
Creditors	**(0.4)**	(0.3)
Net assets	**192.4**	171.1

Sch9A, 11(1) Managed funds are defined as funds of a group pension fund which fall within Class VII of Annex 11.1 to the Interim Prudential Sourcebook for Insurers and which the company administers in its own name on behalf of others and to which it has legal title.

35 Notes to the shareholders' cash flow statement

FRS 1, 12

(a) Reconciliation of profit before tax to net cash inflow from operating activities

	2008	2007 (restated)
	£m	**£m**
Profit on ordinary activities before tax	**81.3**	78.9
Add back: interest charged to operating profit	**5.3**	2.9
Adjustments for non-cash items:		
- Shareholder realised and unrealised investment gains	**(5.0)**	(4.1)
- Amortisation of goodwill	**1.0**	–
- Depreciation of tangible assets	**0.1**	0.1
- Profits relating to long-term business	**(67.6)**	(64.4)
- Allocated investment income	**(10.0)**	(8.1)
- Net cash received from long-term business	**50.0**	46.1
- Movements in other assets/liabilities	**3.5**	(2.2)
Net cash inflow from operating activities	**58.6**	49.2

FRS 1, 35

The reconciliation of operating profit to net cash flows from operating activities should normally take profit or loss on ordinary activities before tax as its starting point.

Insurance companies or groups conducting long-term business may also choose to disclose in the notes to the cash flow statement an analysis of the cash flows of the long-term business.

FRS 1, 56

It is not mandatory to analyse cash flows between continuing and discontinued business. However such analysis is encouraged by FRS 1. Proforma-Life Limited has no discontinued business.

The example for an insurance group in the appendix to FRS1 includes this optional disclosure.

(b) Movement in portfolio investments, net of financing

	2008
	£m
Decrease in cash holdings	**(20.3)**
Cash outflow on portfolio investments	**(15.1)**
Increase in loans	**(47.2)**
Movement arising from cash flows	**(82.6)**
Movement in long-term business cash flows	**134.8**
Acquired with subsidiary	**136.1**
Changes in market value and currencies	**2.3**
Total movements in portfolio investments, net of financing	**190.6**
Portfolio investments, net of financing at 1 January 2008	**1,609.2**
Portfolio investments, net of financing at 31 December 2008	**1,799.8**

FRS 1, 48

Comparative figures are not required for the note to the statement that analyses changes in the balance sheet amounts making up portfolio investments less financing or the note of the material effects of acquisitions and disposals of subsidiary undertakings.

(c) Cash flows invested in portfolio investments

	2008	2007
	£m	**£m**
Purchase of portfolio investments		
- Shares and other variable-yield securities	**5.1**	11.9
- Loans, debt securities and other fixed-income securities	**0.5**	1.6
	5.6	13.5
Sale of portfolio investments		
- Shares and other variable-yield securities	**(18.0)**	(2.1)
- Loans, debt securities and other fixed-income securities	**(1.6)**	–
	(19.6)	(2.1)
Net(decrease)/increase in deposits with credit institutions	**(1.1)**	0.8
Net cash (outflow)/inflow on portfolio investments	**(15.1)**	12.2

(d) Movement in cash, portfolio investments and financing

FRS 1, 35

	At 1 Jan 2008	Cashflow	Long-term business	Acquired with subsidiary (excluding cash)	Changes to market values and currency	At 31 Dec 2008
	£m	£m	£m	£m	£m	£m
Net cash at bank and in hand	88.2	(20.3)	(20.9)	–	–	**47.0**
Land and buildings	172.1	–	8.2	–	–	**180.3**
FRS 1, 36 Shares and other variable-yield securities	988.2	(12.9)	226.0	56.0	2.0	**1,259.3**
Loans, debt securities and other fixed income securities	347.3	(1.1)	(57.9)	80.1	0.3	**368.7**
Deposits with credit institutions	53.2	(1.1)	(20.5)	–	–	**31.6**
Other portfolio investments	10.2	–	0.2	–	–	**10.4**
Borrowings	(50.0)	(47.2)	(0.3)	–	–	**(97.5)**
	1,609.2	(82.6)	134.8	136.1	2.3	**1,799.8**

Net cash at bank and in hand includes overdrafts repayable on demand of £15.1m (2007: £4.1m) which are included within 'amounts owed to credit institutions' in the consolidated balance sheet. The borrowings analysis above excludes these amounts.

(e) Analysis of cash flows on acquisition of subsidiary undertaking

	2008
	£m
Net cash acquired with subsidiary undertaking	**1.4**
Portfolio investments less financing acquired with subsidiary undertaking	**136.1**
Other net liabilities	**(72.1)**
	65.4
Goodwill	**30.1**
Satisfied by cash consideration	**95.5**

The subsidiary undertaking acquired during the year contributed £0.7m to the Group's net operating cash flows.

FRS 1, 45

Material effects on amounts reported under each of the standard headings reflecting the cash flow of a subsidiary undertaking acquired or disposed of in the period should be disclosed as far as practicable. This information could alternatively be given by dividing cash flows between continuing and discontinued operations and acquisitions.

36 Pension costs

FRS 17, 77(a)

The Group operates a funded scheme of the defined benefit type with assets held in separate trustee-administered funds to meet long-term pension liabilities to past and present employees. . The scheme provides retirement benefits on the basis of members' final salary. The trustees of the fund are required to act in the best interest of the fund's beneficiaries. The appointment of trustees to the fund is determined by the scheme's trust documentation. The Group has a policy that on-third of all trustees should be nominated by members of the fund, including at least one member by current pensioners.

In addition to its statutory duties the board of trustees have been granted the power to 'call' for additional contributions in the event of certain circumstances. The circumstances in which the trustees can exercise this power include a disposal that accounts for more than 15% of the net assets, as reported in the consolidated balance sheet or when the funding position of the scheme falls below 65% of the scheme liabilities.

An actuarial valuation of the Group pension scheme, using the projected unit basis, was carried out at 31 December 2008 by Ham & Timberlake, independent consulting actuaries.

The principal assumptions used by the actuaries were:

FRS 17, 77(m)

	2008	2007
Inflation assumption	**2.8%**	2.5%
Rate of increase in salaries	**4.3%**	4.0%
Rate of increase in pensions in payment	**3.0%**	4.0%
Discount rate	**5.2%**	5.0%
Mortality assumptions:		
Longevity at age 65 for current pensioners		
- Men	**22.5 years**	22.3 years
- Women	**24.8 years**	24.3 years
Longevity at age 65 for future pensioners		
- Men	**24.8 years**	24.5 years
- Women	**26.8 years**	26.5 years

FRS 17, 77 (i), (m)

The assets in the scheme and the expected rate of return were:

	Long-term rate of return expected for 2008	Value at 31 December 2008	Long-term rate of return expected for 2007	Value at 31 December 2007
		£m		£m
Equities	**8.2%**	**26.3**	8.4%	25.1
Bonds	**4.9%**	**8.8**	5.6%	8.6
Total market value of assets		**35.1**		33.7
Present value of scheme liabilities *		**(31.9)**		**(30.7)**
Surplus in scheme *		**3.2**		3.0
Related deferred tax liability *		**(1.0)**		**(0.9)**
Net pension asset *		**2.2**		2.1

* The reconciliation element of the table above is not mandatory under FRS 17.

PwC

The equity investments and bonds which are held in scheme assets are quoted and are valued at the current bid price following the adoption of the amendment to FRS 17. Previously these were valued at mid-market price. The effect of this change is that the value of scheme assets at 31 December 2007 has been restated from £34.3m to £33.7m, a decrease of £0.6m.

FRS 17, 77(b)

	2008	2007
Reconciliation of present value of scheme liabilities	**£m**	**£m**
At 1 January	**30.7**	29.1
Current service cost	**2.4**	2.2
Past service cost	**-**	-
Interest cost	**1.7**	1.6
Benefits paid	**(3.2)**	(3.0)
Net actuarial loss	**0.3**	0.8
At 31 December	**31.9**	30.7

FRS 17, 77(n)

Sensitivity analysis of scheme liabilities

The sensitivity of the present value of scheme liabilities to changes in the principal assumptions used is set out below:

	2008	2007
	Change in assumption	**Impact on scheme liabilities**
Discount rate	**Increase/decrease by 1%**	Increase/ decrease by 8.5%
Rate of inflation	**Increase/decrease by 1%**	Increase/ decrease by 5.0%
Rate of increase in salaries	**Increase/decrease by 1%**	Increase/ decrease by 3.0%
Rate of increase in pensions in payment	**Increase/decrease by 1%**	Increase/ decrease by 3.0%
Mortality	**Increase by 1 year**	Increase by 4.5%

FRS 17, 77(d)

Reconciliation of fair value of scheme assets	2008 £m	2007 (restated) £m
At 1 January	**33.7**	32.8
Expected return on plan assets	**2.4**	2.5
Contributions paid by employer	**2.6**	2.6
Benefits paid	**(3.2)**	(3.0)
Actuarial gains / (losses)	**(0.4)**	(1.2)
At 31 December	**35.1**	33.7

FRS 17, 77(j) Scheme assets do not include any of Proforma-Life Limited's own financial instruments or any property occupied by Proforma-Life Limited.

FRS 17, 77(k) The expected return on scheme assets is determined by considering the expected returns available on the assets underlying the current investment policy. Expected yields on fixed interest investments are based on gross redemption yields as at the balance sheet date. Expected returns on equity and property investments reflect long-term real rates of return experienced in the respective markets.

FRS 17, 77(l) The actual return on scheme assets in the year was £2.6m (2007: £2.0m).

		2008 £m	2007 £m
	Analysis of amount charged to operating profit (included in Net operating expenses)		
FRS 17, 77(f)	Current service cost	**2.4**	2.2
FRS 17, 77(f)	Past service cost	**–**	–
	Total operating charge	**2.4**	2.2
	Analysis of amount credited to operating profit (included in Other finance income)		
FRS 17, 77(f)	Expected return on pension scheme assets	**2.4**	2.5
FRS 17, 77(f)	Interest cost on pension scheme liabilities	**(1.7)**	(1.6)
	Net return	**0.7**	0.9
	Analysis of amount recognised in statement of total recognised gains and losses		
FRS 17, 77(g)	Actual return less expected return on pension scheme assets	**0.2**	(0.5)
FRS 17, 77(g)	Experience gains and losses arising on scheme liabilities	**–**	(0.5)
FRS 17, 77(g)	Changes in assumptions underlying the scheme liabilities	**(0.3)**	0.4
	Actuarial (loss)/gain	**(0.1)**	(0.6)

FRS 17, 77(h) The cumulative amount of actuarial losses recognised in the statement of total recognised gains and losses is £2.4m (2007: £2.3m).

FRS 17, 77(p) The full actuarial valuation at 31 December 2008 showed a small increase in the surplus in the scheme from £3.0m at 31 December 2007 to £3.2m. No additional improvements in benefits were made in either 2008 or 2007. As a result of the small surplus at 31 December 2007, it was agreed with the actuaries and trustees of the pension scheme that from 1 January 2008 contributions would continue to be made to the pension scheme at a rate of 7% of pensionable salaries (2007: 7%). It has been agreed with trustees that contributions will remain at that level for the next three years. As a result, the total contributions expected to be made to the scheme by Proforma-Life Limited in the year to 31 December 2009 is £6.6m.

		2008	2007 (restated)	2006 (restated)	2005	2004
FRS 17, 77(o)	**History of experience gains and losses**					
	Difference between expected and actual return on scheme assets					
	▪ Amount (£m)	**0.2**	(0.5)	(0.3)	(0.5)	(0.2)
	▪ Percentage of scheme assets	**0.6%**	(1.5%)	(1.3%)	(1.6%)	(1.3%)
	Experience gains and losses on scheme liabilities					
	▪ Amount (£m)	**–**	(0.5)	(0.3)	(0.4)	(0.4)
	▪ Percentage of scheme liabilities	**0.0%**	(1.6%)	(1.2%)	(1.4%)	(1.5%)
	Total actuarial (loss)/gain					
	▪ Amount (£m)	**(0.1)**	(0.4)	(0.9)	(0.9)	(1.1)
	▪ Percentage of scheme liabilities	**(0.3%)**	(1.3%)	(3.6%)	(3.2%)	(4.1%)

FRS 17, 95C Proforma-Life Limited has elected not to restate amounts for 2005 and 2004, as permitted by the amendment to FRS 17.

FRS 17 ' Retirement benefits'

PwC FRS 17 does not explicitly consider the requirements of companies that prepare accounts under Schedule 9A. However, the ABI SORP provides guidance.

Treatment of the charge for the year

The charge/credit relating to the pension fund is taken to three separate areas in the performance statement:

ABI, 229
- current and any past service costs of a defined benefit scheme should be included under the appropriate headings in the profit and loss account;

ABI, 230
- the difference between the interest costs and the expected investment return on pension fund assets should be included as appropriate in the Technical account - long-term business or the Non-technical account as a new line within Investment income/charges; and

ABI, 231
- the Statement of total recognised gains and losses (STRGL) should show actuarial gains/losses attributable to shareholders showing:
  - differences between the expected return on the scheme assets and the actual return;
  - the impact of experience variations on the scheme liabilities and the effect of changes in assumptions; and
  - adjustments due to limits on the amount that can be recognised as a pension fund asset in the balance sheet.

ABI, 232 Any movement in these gains/losses not attributable to shareholders should be included as a separate line in the Technical account – Long-term business. This should be placed immediately above the line for 'Transfer to or from the Fund for future appropriations' and reflected in that transfer.

Balance sheet

ABI, 233 A pension asset or liability should be shown as the last item of the assets or liabilities section as appropriate. A sub-total of assets or liabilities should be disclosed immediately before the pension fund asset or liability.

ABI, 234 Where the FFA is determined after taking account of a pension asset or a pension liability, the impact should be disclosed separately in the notes to the accounts.

ABI, 235 The methodology used for the calculation of the longer term rate of investment return on pension scheme assets should be consistent with any method used for the calculation of the longer term rate of investment return for insurance business.

Treatment in group situations

ABI, 236 In the case of groups, individual companies may not be able to identify their share of pension assets or liabilities. They are allowed to account for it as a defined contribution scheme but must disclose:

- the fact that the scheme is a defined benefit scheme and they are unable to identify their share of assets and liabilities; and
- any available information about the existence of the surplus or deficit in the scheme and its implications for the employer.

ABI, 237 The consolidated accounts should show the group scheme as a defined benefit scheme. The allocation of the surplus/deficit between that attributable to shareholders and to funds not allocated to either shareholders or policyholders (i.e. the FFA) should reflect the extent to which each benefits or is disadvantaged. Sufficient disclosure should be made to enable the accounting treatment to be understood.

Long-term business provision

ABI, 183 Policyholder liabilities in an insurer's regulatory returns may implicitly take account of a pension fund surplus through reduced expense assumptions. Where the long-term business provision is based on the regulatory returns, the effect of this adjustment to expense assumptions should be reversed in order to avoid double-counting the pension fund surplus.

Death-in-service and incapacity benefits

UITF 35 Where death-in-service and incapacity benefits are provided through a defined benefit pension scheme and are not wholly insured, the uninsured scheme liability and the cost of the accounting period should be measured using the projected unit method, in line with other retirement benefits. The valuation of uninsured benefits therefore reflects the current period's portion of the full benefits ultimately payable in respect of current members of the scheme. The cost of insured benefits is determined by the relevant insurance premiums. This is not applicable to Proforma-Life Limited.

Amendment to FRS 17 'Retirement benefits'

Amendment to FRS 17 On 7 December 2006, the ASB published an amendment to FRS 17, 'Retirement benefits', which aligns FRS 17's disclosure requirements with those contained in IAS 19, 'Employee benefits'. The amendment is effective for periods beginning on or after 6 April 2007.

Proforma-Life Limited has adopted this amendment.

The principal changes introduced by the Amendment include:

- quoted securities to be valued at 'current bid price' rather than 'mid-market value';
- in a multi-employer scheme, where companies are unable to identify their share of the underlying assets and liabilities, the reason why sufficient information is not available to account for the scheme as a defined benefit scheme should be disclosed;
- other additional disclosures include:
  - information that enables users of the financial statements to evaluate the nature of the entity's participation in defined benefit schemes and the financial effects of changes in those schemes (previously only the nature of schemes had to be disclosed);
  - principal actuarial assumptions (including mortality rates);

- reconciliation of opening and closing balances of scheme assets and of scheme liabilities;
- analysis of scheme liabilities into amounts arising from schemes that are wholly unfunded and those that are wholly or partly funded;
- amounts included in scheme assets for each category of the entity's own financial instruments and any property occupied by, or other assets used by, the entity;
- best estimate of contributions expected to be paid to scheme during accounting period beginning after balance sheet date; and
- sensitivity analysis on retirement healthcare obligation and costs.

- the following disclosures are no longer required:
  - date of most recent actuarial valuation and if the actuary is an employee or officer of the company;
  - effects of changes in demographic and financial assumptions underlying the present value of the scheme liabilities;
  - financial assumptions at the beginning of the period;
  - analysis of reserves distinguishing the amount relating to the defined benefit asset or liability net of the related deferred tax;
  - for closed schemes and those in which the age profile of the active membership is rising significantly, the fact that under the projected unit method the current service cost will increase as the members of the scheme approach retirement;
  - the expected rate of return assumed for each class of scheme assets;
  - FRS 17 previously required disclosure of the assumptions used at the beginning of the previous period, the beginning of the current period and at the balance sheet date. The amendment to FRS 17 requires disclosure of the assumptions *used as at* the balance sheet date. Therefore, disclosure will no longer be given of assumptions for a three year period. For most assumptions, this means that the disclosure will be given of figures at the balance sheet date (and comparatives). However, for the expected rate of return, the ASB notes in a footnote that the disclosure will be given of figures at the beginning of the period (and comparatives).

ASB Best practice reporting statement: Retirement benefits: - Disclosures

ASB Best Practice Reporting Statement

The ASB has published a 'best practice reporting statement' on disclosures related to retirement benefit schemes, which can be applied equally to UK GAAP (includes the Amendment to FRS 17 mentioned above) and IFRS reporters. The reporting statement sets out principles for disclosure, rather than specific requirements, allowing entities the flexibility to provide disclosures that are appropriate to their individual exposure to risks arising from defined benefit schemes. Proforma-Life Limited has not adopted this statement. The main areas where further disclosures are encouraged are:

- Explanation of the relationship between the reporting entity and the trustees (managers) of the defined benefit scheme
- Disclosure of principal actuarial assumptions
- Sensitivity analysis of the principal assumptions used to measure scheme liabilities
- How the liabilities arising from defined benefit schemes are measured
- Future funding obligations in relation to the schemes
- Nature and extent of the risks arising from financial instruments held by the defined benefit scheme

37 Guarantees and financial commitments

(a) Operating lease commitments

The Group has annual commitments in respect of non-cancellable operating leases as follows:

		Land and buildings		Other	
		2008	**2007**	**2008**	**2007**
		£m	**£m**	**£m**	**£m**
SSAP 21, 56	Operating leases which expire:				
	- Within one year	**–**	0.1	**0.1**	0.1
	- Between one and five years	**0.4**	0.3	**0.2**	0.2
	- After five years	**0.9**	0.6	**–**	–
		1.3	1.0	**0.3**	0.3

(b) Other financial commitments

		Group	
		2008	**2007**
		£m	**£m**
Sch9A, 70(5)	Contracts placed for future property-related revenue expenditure not provided in the financial statements	**1.2**	0.2

(c) Contingent liabilities

FRS 12, 91
Sch9A 70(2)

The Group has contingent liabilities in respect of uncalled capital on certain investments amounting to £10.1m (2007: £15.2m).

FRS 12, 3(c) The requirements relating to the disclosure of contingent assets and liabilities are set out in FRS 12. Whilst insurance entities are exempt from the requirements in respect of contingencies arising from contracts with policyholders, they are not exempt in respect of other contingencies, for example potential levies to be raised by the Financial Services Compensation Scheme.

FRS 12, 27, 31 Under FRS 12 neither contingent assets nor contingent liabilities should be recognised in the balance sheet.

FRS 12, 91 Unless the possibility of any loss is remote, disclosure should be made for each class of contingent liability of the nature of the liability together with, where practicable, an estimate of its financial effect, an indication of any uncertainty relating to the amount or timing of any outflow, and the potential for any reimbursement.

FRS 12, 34 Only where an inflow of economic benefit is probable should disclosure of the nature and quantum of contingent assets be given.

38 Policyholder redress

The long-term business provision includes an amount of £30 million (2007: £25m) in respect of potential redress and associated costs that may be required in respect of past sales of certain long-term products. There is no industry wide review of sales of such products and the level of redress required is uncertain, being dependent on the volume of complaints received in the future and the results of the investigation of these complaints. The movement in the amount provided during the year was due to redress payments of £3m being made and an additional £8m being provided. During the year, Proforma-Life Limited was fined £325,000 by the Financial Services Authority following a review of complaints handling procedures in this area. As a result of this review procedures in this area have been enhanced.

FRRP PN51 In a 1998 pronouncement, the FRRP confirmed that companies should consider the need to disclose fines in order for the accounts to show a true and fair view. The determinants of the materiality of an item are size, nature and circumstances. Where an item, such as a fine, is considered to be material by virtue of this guidance, it would be normally treated as an exceptional item under FRS 3. It would therefore be disclosed with a description adequate to enable its nature to be understood.

INSPRU 1.5.33R The FSA's rules prevent proprietary firms from paying any financial penalties imposed by the FSA from a long-term insurance fund.

In June 2008 the FSA issued consultation paper 08/11: With-profits funds – Compensation and redress. The consultation proposes that proprietary insurance companies will no longer be permitted to charge compensation for mis-selling to inherited states of with-profit funds. A policy statement by the FSA is expected in the first quarter of 2009.

PwC FRS 12 'Provisions, contingent liabilities and contingent assets' does not apply to contracts between insurers and their policyholders. However, the principles in FRS 12 regarding provisioning and disclosure may be viewed as best practice when considering policyholder redress.

FRS 8, 6

39 Related party transactions

Transactions involving directors and key management
No contract of significance existed at any time during the year in which a director or key manager was materially interested or which requires disclosure as a related party transaction.

OEIC Funds
During the year, the long-term business funds of the Group have invested in a number of OEIC funds managed by Proforma-Life Mutual Fund Management Limited, a subsidiary of the Group. As at 31 December 2008 the value of such shares held by the long-term business funds was £53.2m (2007: £48.1m).

Related party disclosures

FRS 8, 3 Under FRS 8, transactions and balances with related parties must be disclosed. There is no requirement to disclose in consolidated financial statements balances and transactions that are eliminated on consolidation. Where the company is a 90% subsidiary, there is also an exemption from disclosing transactions (but not balances) with other members of the parent company's group.

FRS 8, 20
PwC Disclosure is only required in respect of material transactions, being transactions which might reasonably be expected to influence decisions made by the users of general purpose financial statements. However, where the party in question is a director or key manager (or a member of a director's or key manager's close family or an entity controlled by a director or key manager or a member of their close family) materiality must be considered in relation to both parties. Disclosure should be made irrespective of whether or not an arms-length price is charged. Some transactions with the life fund are not eliminated on consolidation (for example, where a group has a service company transacting with the life fund). Such transactions should be disclosed in the financial statements.

40 Ultimate parent company

FRS 8, 5
Sch5, 30, 31

The directors regard Proforma-US Inc, a company incorporated in the USA, as the immediate and ultimate parent company and ultimate controlling party. Copies of the consolidated financial statements of Proforma-US Inc can be obtained from The Secretary, Proforma-US Inc, 589 Fourth Avenue, New York, 59361.

FRS 8, 3

Advantage has been taken of the exemption in FRS 8 not to disclose transactions with entities that are part of the Proforma-US Inc group.

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