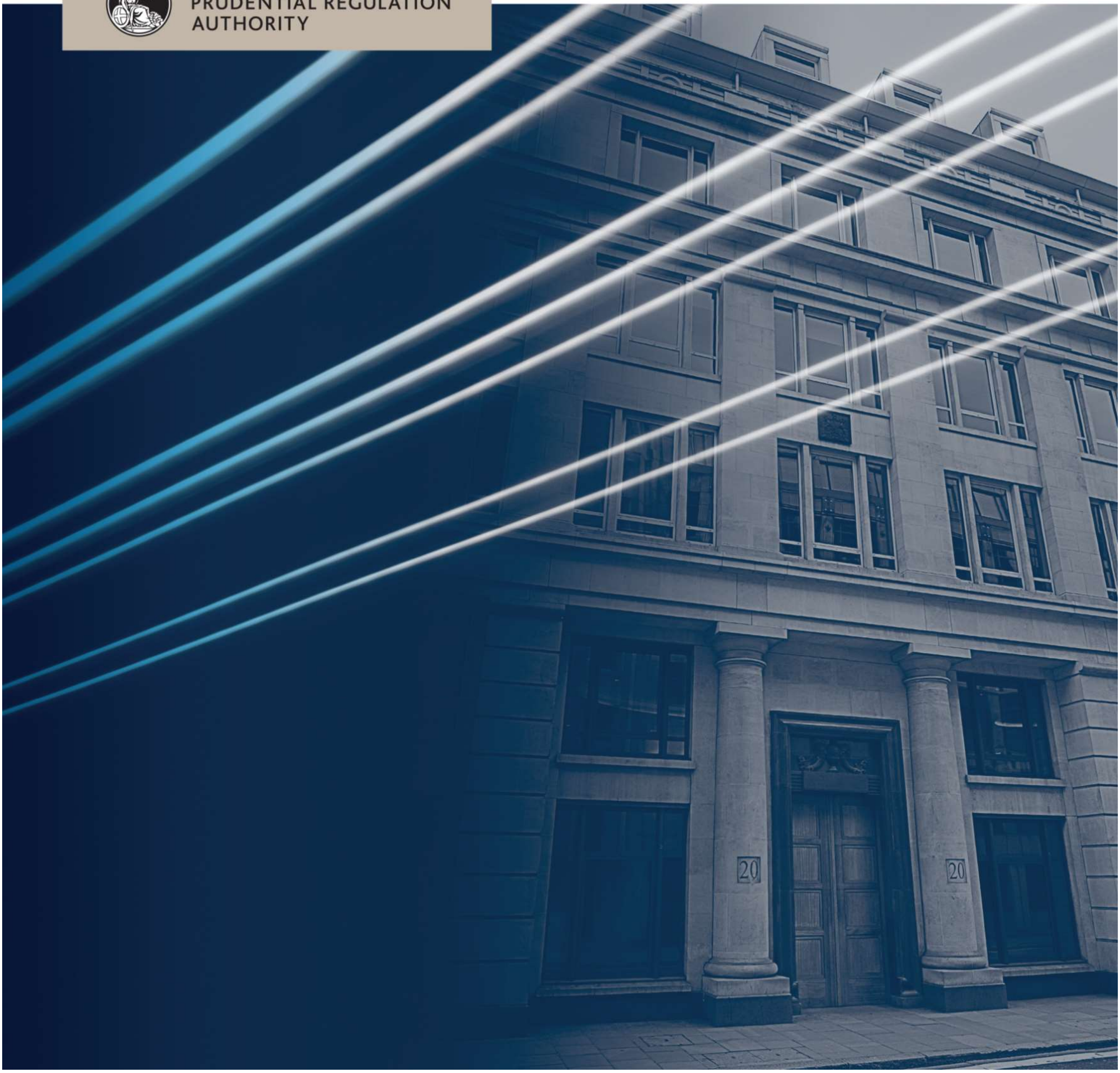
Supervisory Statement | SS38/15

Solvency II: consistency of UK generally accepted accounting principles with Solvency II

November 2024

(Updating August 2015)

BANK OF ENGLAND
PRUDENTIAL REGULATION AUTHORITY



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Contents

1 Introduction

1.1 This supervisory statement is addressed to all insurance firms within the scope of Solvency II reporting under UK generally accepted accounting principles (GAAP) rather than using international accounting standards (IFRS).

1.2 The statement was subject to public consultation,[1] and reflects feedback received by the PRA. Some comments suggested altering wording and these suggestions have been accepted where clarity would be improved. There is no change in policy.

1.3 The PRA is publishing this statement to expand on its general approach as set out in its Insurance Approach document.[2] By clearly and consistently explaining its views in this area, the PRA seeks to advance its statutory objectives of ensuring the safety and soundness of the firms it regulates, and contributing to securing an appropriate degree of protection for policyholders.

1.4 The PRA has considered matters to which it is required to have regard, and it considers that this statement is compatible with the Regulatory Principles and relevant provisions of the Legislative and Regulatory Reform Act 2006. This statement is not expected to have any direct or indirect discriminatory impact under existing UK law.

1.5 Rule 5.4 in the Valuation Part of the PRA Rulebook contains a derogation ('the derogation') for firms within the scope of Solvency II for which annual financial statements and consolidated financial statements (if any) are prepared under UK generally accepted accounting principles. This allows firms the option of recognising and valuing assets and liabilities under UK GAAP for Solvency II purposes if:

- UK GAAP is consistent with Chapter 2 of the Valuation Part of the PRA Rulebook;
- the valuation method is proportionate to the nature, scale, and complexity inherent in the business of the undertaking; and
- the process of valuing the assets and liabilities using international accounting standards would impose costs which are disproportionate with respect to the total administrative expenses of the firm.

1.6 The PRA expects that where UK GAAP and IFRS are consistent, in that they apply the same requirements as regards recognition and valuation, the derogation will not apply. In such cases firms will not incur any costs to use IFRS recognition and valuation criteria, since they will already be applying what IFRS would require when reporting under UK GAAP.

1.7 The PRA expects any firm wishing to take advantage of the derogation to provide supporting evidence regarding the second and third conditions set out in paragraph 1.5 above to its supervisor before so doing. However, rather than each firm having individually to consider and establish whether its proposed accounting treatment is consistent with Chapter 2 of the Valuation Part, and in order to promote consistency in application of the derogation, this supervisory statement lists those UK GAAP treatments which the PRA considers to be consistent with Chapter 2 of the Valuation Part, in full or in part.

1 www.bankofengland.co.uk/pra/Pages/publications/cp/2015/cp1615.aspx
2 https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/approach/insurance-approach-2023.pdf

1.8 The derogation relates to Valuation 5.1 and 5.2, but does not affect the application of Valuation 6 to 12 except to the extent that these provisions refer back to Valuation 5 regarding recognition or valuation. Therefore in addition to Valuation 5:

	The derogation:
Valuation 6: Valuation Methodology – Valuation Hierarchy	• Applies to the whole of Valuation 6.
Valuation 10: Valuation Methods for Specific Liabilities	• applies to the first sentence of Valuation 10.1. [The second sentence of Valuation 10.1 reiterates requirement in Valuation 2.2, and as such cannot be derogated.] • does not apply to Valuation 10.2.
Valuation 11: Deferred Taxes	• applies to Valuation 11.1, but not to Valuation 11.2 or Valuation 11.3.

1.9 Any firm that relies on the derogation will still be expected to apply in full the remaining valuation requirements of the PRA Rulebook, regardless of whether the UK GAAP provisions are consistent with Chapter 2 of the Valuation Part.

1.10 For insurance firms, most of the differences between UK GAAP and international accounting standards relate only to the level of detail which must be disclosed. Since the derogation addresses recognition and valuation of assets and liabilities rather than their disclosure, it is expected to have a limited effect in the United Kingdom.

2 Consistency of Chapter 2 of the Valuation Part with UK GAAP to which the derogation may apply

2.1 The PRA has analysed the financial reporting standards (FRS) to consider whether these are consistent with Chapter 2 of the Valuation Part and therefore within the possible scope of the derogation. Its conclusions are set out in the table below.

2.2 Where a firm is discussing with its usual supervisor contact whether the conditions for an application of the derogation apply, the PRA expects that firm to apply this supervisory statement's conclusions on FRS consistency with Chapter 2 of the Valuation Part as regards which provisions of UK GAAP it may use.

	Derogation permits use of FRS?	**Reason**
FRS 100	n.a.	Provisions do not contain valuation methodologies.
FRS 101	n.a.	Provisions do not contain valuation methodologies that differ from IFRS.
FRS 102		
Chapters 1-10	n.a.	Provisions do not contain valuation methodologies.
Chapter 11: Basic financial instruments	Yes, with amendments	**Assets**: The fair value measurement methodology is consistent with Chapter 2 of the Valuation Part. **Liabilities**: The fair value measurement methodology is consistent with Chapter 2 of the Valuation Part when an item is initially recognised. Subsequently, the second sentence of Valuation 10.1; there shall be no valuation adjustment to take account of the change in own credit standing of the insurance or reinsurance undertaking.
Chapter 12: Other financial instruments	Yes, with amendments	The fair value measurement methodology is consistent with Chapter 2 of the Valuation Part when an item is initially recognised. Subsequently, the second sentence of Valuation 10.1 applies; there shall be no valuation adjustment to take account of the change in own credit standing of the insurance or reinsurance undertaking.
Chapter 13: inventories	No	Valuation 12.5 still applies.
	Derogation permits use of FRS?	**Reason**

Chapter 14: investment in associates	No	Valuation 9 still applies.
Chapter 15: Investment in joint ventures	No	Valuation 9 still applies.
Chapter 16: Investment property	Yes, for one valuation option	Only the fair value model methodology is consistent with Chapter 2 of the Valuation Part.
Chapter 17: Property plant and equipment	Yes, for one valuation option	Only the revaluation model is consistent with Chapter 2 of the Valuation Part.
Chapter 18: Intangibles other than goodwill	No	Valuation 8.1 still applies.
Chapter 19: Business combinations and Goodwill	Yes, in part	**Business combinations** — Acquisition accounting: the fair value valuation is consistent with Chapter 2 of the Valuation Part. **Goodwill** — Valuation 8.1 still applies.
Chapter 20: Leases	No	Valuation 12.4 still applies.
Chapter 21: Provisions and contingencies	No, because Valuation 5.4(4) does not apply	**Provisions and contingent** assets — provisions consistent with IFRS valuation methodology so using IFRS would not impose any additional costs. **Contingent liabilities** — Valuation 7 still applies.
Chapter 22: Liabilities and equity	No	Solvency II regulatory capital is not dependent on accounting treatment.
Chapter 23: Revenue recognition	n.a.	Provisions do not contain valuation methodologies.
Chapter 24: Government grants	Yes	Both the recognition and fair value measurement are consistent with Chapter 2 of the Valuation Part.
Chapter 25: Borrowing costs	No	Provisions are based on a cost model so are not consistent with Chapter 2 of the Valuation Part.
Chapter 26: Share based payments	Yes	This fair value valuation methodology is consistent with Chapter 2 of the Valuation Part.
Chapter 27: Impairment of assets	No	Provisions are based on a cost model so are not consistent with Chapter 2 of the Valuation Part.
Chapter 28: Employee benefits	Yes	The measurement principles for employee benefits are consistent with Chapter 2 of the Valuation Part.

Chapter 29: Income tax	No, because Valuation 5.4(4) does not apply	**Tax** — provisions consistent with IFRS valuation methodology so using IFRS would not impose any additional costs. **Deferred tax** — Provisions are consistent with IFRS as regards Valuation 11.1 so using IFRS would not impose disproportionate costs. Valuation 11.2 and 11.3 still apply.
Chapter 30: Foreign currency translation	No, because Valuation 5.4(4) does not apply	Provisions consistent with IFRS valuation methodology so using IFRS would not impose any additional costs.
Chapter 31: Hyperinflation	Yes	The figures of current and corresponding prior periods are restated in terms of the measuring unit current at the end of the reporting period, which is consistent with Chapter 2 of the Valuation Part.
Chapter 32	No, because Valuation 5.4(4) does not apply	**Events after the End of the Reporting Period** — Provisions are consistent with IFRS valuation methodology so using IFRS would not impose any additional costs
Chapter 33	n.a.	Provisions do not contain valuation methodologies.
Chapter 34: Specialist activities		
Agriculture	Yes, (in part)	Fair value less cost to sell is consistent with Chapter 2 of the Valuation Part where estimated cost to sell is immaterial. If costs to sell are material, then the adjustment required by Valuation 12.7 should be applied.
Extraction activities	n.a.	PRA does not expect these provisions to apply to insurance undertakings.
Service concession arrangements	n.a.	PRA does not expect these provisions to apply to insurance undertakings.
Financial Institutions	n.a.	Provisions do not contain valuation methodologies.
Retirement benefit plans	n.a.	PRA does not expect these provisions to apply to insurance undertakings.
Heritage assets	n.a.	PRA does not expect these provisions to apply to insurance undertakings.
Funding commitments	In part, with amendments	**Liabilities** — Where the funding commitment is a liability the fair value measurement methodology is consistent with Chapter 2 of the Valuation Part at the point the funding commitment is initially recognised. Subsequently, there shall be no valuation adjustment to take account of the change in own credit

		standing of the insurance or reinsurance undertaking. **Contingent liabilities** — Where the funding commitment is a contingent liability Valuation 7 still applies.
Income resources from non-exchange transactions	Yes	The fair value valuation basis is consistent with Chapter 2 of the Valuation Part.
Public benefit entity combinations	n.a.	PRA does not expect these provisions to apply to insurance undertakings.
Public benefit entity concessionary loans	n.a.	PRA does not expect these provisions to apply to insurance undertakings.
Chapter 35	No	This chapter provides transitional provisions from the previous UK GAAP regime.
FRS 103	No	Chapters 2 to 14 of the Technical Provisions, the Technical Provisions – Further Requirements and the Matching Adjustment Parts of the PRA Rulebook still apply.

Annex – updates to SS38/15

This annex details changes made to SS38/15 following its initial publication in August 2015 following Policy Statement (CP) 16/15 'Solvency II: consistency of UK generally accepted accounting principles with the Solvency II Directive'.

15 November 2024

This SS has been updated alongside the publication of Policy Statement (PS) 15/24 - Review of Solvency II: Restatement of assimilated law.[3] This includes updating all previous references to the Commission Delegated Regulation (EU) 2015/35 so as to now refer to the relevant rule(s) in the PRA Rulebook.

These changes are limited to those necessary following the restatement the Solvency II regime into PRA policy material, and do not include an updated analysis of the UK GAAP and IFRS regimes.

3 www.bankofengland.co.uk/prudential-regulation/publication/2024/november/review-of-solvency-ii-restatement-of-assimilated-law-policy-statement.